

MEDIKA d.d.

**AUDITOR'S REPORT AND
CONSOLIDATED FINANCIAL STATEMENTS
31 DECEMBER 2012**

This version of the financial statements is a translation from the original, which was prepared in the 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 the financial statements takes precedence over this translation.

	Page
Annual report	1 - 3
Statement of the Management and Supervisory Board's responsibilities	4
Independent Auditor's Report to the shareholders of Medika d.d.	5
Consolidated statement of comprehensive income	6
Consolidated statement of financial position	7
Consolidated statement of changes in equity	8
Consolidated statement of cash flows	9 - 10
Notes to the consolidated financial statements	11 - 49

ANNUAL REPORT

Operating result in 2012

In the year 2012, Medika Group realized consolidated revenue in the amount of HRK 2,244,484 thousand, an increase of 3.3% . Consolidated operating profit amounts to HRK 67,567 thousand which is a 39.7 % increase in comparison to prior year.

Consolidated profit before tax amounts to HRK 51,611 thousand and consolidated net profit HRK 48,270 thousand, which is an increase of HRK 29,879 thousand in comparison to prior year.

The Management of the Company adopted a decision to reinvest profits for the purpose of long-term goals of encouraging investment in the amount of HRK 33,817 thousand, which will be registered during 2013 as an increase of the Company's share capital. Increase of share capital will be carried out by increasing the nominal value of the shares, which means that existing shareholder rights will not change, and will belong to the shareholders in proportion to their previous participation in the share capital.

If analysing operating business segments (note 6 in financial statements), 62.7% of total consolidated income was generated through "pharmacies" segment, of which 14.2% from own pharmacies and 23.5% through "hospitals" segment. In comparison to prior year, the "hospitals" segment share in total consolidated revenue experienced no change while at the same time the "pharmacies" segment share fell by 1.1% in total consolidated revenue.

Total consolidated assets amount to HRK 2,017,879 thousand, and have increased by 8.5% in comparison to prior year. Consolidated current assets comprise 79.9% of total assets. Trade and other receivables are the most significant part of total assets and have increased by 11.8% in comparison to prior year.

In accordance with the incorporation agreement of Litmus d.o.o., the Company invested its ownership interest in Primus nekretnine d.o.o. into the share capital of Litmus d.o.o. An independent valuer estimated the value of Primus nekretnine d.o.o. at HRK 18,698 thousand. As a result of this, the Group recognized a gain of HRK 7,470 thousand. In addition, the Company increased the capital of Litmus d.o.o. by cash of HRK 450 thousand, which results in the Company owning 41.53% of Litmus d.o.o.

Group's equity to assets ratio shows that 19% of total consolidated assets are financed through own resources.

Total consolidated credit indebtedness of the Medika Group is HRK 331,074 thousand, of which HRK 194,097 thousand relates to short-term loans (loans and finance lease), while the remainder in the amount of HRK 136,977 thousand relates to long-term loans and finance lease (note 26).

Consolidated financial results are presented in the statement of comprehensive income on page 6 of the financial statements.

Subsequent events

There are no events after the reporting date that require adjustment of the financial statements or additional disclosures in the financial statements.

The vision of company development

The business plan of Medika d.d. for 2013 anticipates annual growth of sales of 2%, with further growth potential in following years. In accordance with the growth of sales, an increase in market share is planned. The Company will continue with its core business: distribution of pharmaceuticals and medical products and will strongly develop operations with products that represent the core business of the firm.

Number of employees is planned to remain at the current level, with an increase in productivity.

ZU Ljekarne Prima Parme's development strategy is to expand its network of pharmacies to the whole territory of Croatia.

Treasury shares

In June 2012, the Company granted 252 of its treasury shares to key management.

During 2012 the Company has acquired 308 of its treasury shares.

Medika d.d. currently owns 1,640 treasury shares, which represents 5.43% of shares issued.

Subsidiaries and associates

Medika d.d. has a subsidiary Zdravstvena ustanova Ljekarne Prima Parme, registered in Split which is 100% owned by Medika d.d. and an associate Litmus d.o.o., registered in Zagreb, which is 41.53% owned by Medika d.d.

Zdravstvena ustanova Ljekarne Prima Parme itself has subsidiaries: Zdravstvena ustanova Ljekarne Delonga (Okrug Gornji), Zdravstvena ustanova Ljekarne Ines Škoko (Zagreb), Zdravstvena ustanova Ljekarne Atalić (Osijek), Ljekarna Alagić (Split) and Zdravstvena ustanova Ljekarne Čaić (Bošnjaci). These subsidiaries are wholly owned by ZU Ljekarne Prima Parme.

During the year 2012, Ljekarna Dragica Blagus-Vičanović (Strahoninec) has been merged into ZU Ljekarne Prima Parme.

Zdravstvena ustanova Ljekarne Jagatić (Zagreb) is 49% owned by ZU Ljekarne Prima Parme.

Risks

The most significant market risk for Medika d.d. is the long collection period for receivables, especially HZZO (Croatian State Health Insurance) and HZZO related receivables. Therefore, a significant amount of working capital is not available with strong influence on cash flows and timely settlement of Medika d.d. liabilities.

As these receivables are either dependent from or owned by State institutions, risk of bad debt is not considered high. However, this increases the need for additional financing, which increases operating expenses.

Significant risk for Medika d.d. operations is a continuous decrease in the price of prescription medication on the HZZO list and the HZZO administrative approach in determining prices and margins of medication. To lower this risk, Medika d.d. has focused on increasing products which are not limited by law in respect of the price of the product.

Currency risk is a significant financial risk. Majority of inventories are purchased from foreign suppliers in foreign currencies. A portion of loans from commercial banks are settled with foreign currency clause.

Interest risk for the Company arises from short-term and long-term borrowings, with variable interest rate.

Credit risk most significantly arises from trade receivables. Credit risk is higher when dealing with pharmacies, which have more potential going concern issues. Hospitals which have longer collection periods do not have a collection issue and going concern issue.

Corporate governance code

As a listed entity of the Zagreb Stock Exchange, Medika d.d. adopts the corporate governance code of the CFSSA (Croatian Financial Services Supervisory Agency) and the Zagreb Stock Exchange. The corporate governance is published on the web site of the Zagreb Stock Exchange.

The Company has not entered into joint venture, and it does not have securities with special rights nor securities with restriction to vote. There are no cases in which financial rights from securities are separated from ownership of those securities.

Management and Supervisory Board

Management has one member: Mr. Jasminko Herceg, member of the Management Board.

Supervisory Board of the company during the year were as follows: Mr. Mate Perković, president, Mr. Damjan Možina, vice-president, and members: Mr. Matko Bolanča, Mr. Tomislav Gnjidić, Mr. Zlatko Dunković, Mr. Nikica Gabrić and Mrs. Ružica Vadić.

Zagreb, 8 March 2013

Jasminko Herceg
Member of the Management Board

Medika d.d.
ZAGREB, Croatia

MEDIKA d.d.

STATEMENT OF MANAGEMENT AND SUPERVISORY BOARD'S RESPONSIBILITIES

The Management Board is required to prepare the consolidated financial statements for each financial year which give a true and fair view of the financial position of the Group and of the results of its operations and cash flows, in accordance with applicable accounting standards, and is responsible for maintaining proper accounting records to enable the preparation of such financial statements at any time. The Management Board has the responsibility of taking steps which are reasonably available to it in order to safeguard the assets of the Group and to prevent and detect fraud and other irregularities. The Management Board is responsible for selecting suitable accounting policies to conform with applicable accounting standards and then apply them consistently; make judgements and estimates that are reasonable and prudent; and prepare consolidated financial statements on a going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Management Board is responsible for the submission of its annual report together with the annual consolidated financial statements to the Supervisory Board, following which the Supervisory Board is required to approve the annual consolidated financial statements for submission to the General Assembly of Shareholders for adoption.

The financial statements set out on pages 6 to 49 were authorised by the Management Board on 8 March 2013 for issue to the Supervisory Board and are signed below to signify this.

By order of the Management Board

Jasminko Herceg
Member of the Management Board




Medika d.d.
ZAGREB Capital market



Independent auditor's report to the shareholders of Medika d.d.

We have audited the accompanying consolidated financial statements of Medika d.d. ("the Company"), which comprise the consolidated statement of financial position as at 31 December 2012, the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidates Financial Statements

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

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Company as at 31 December 2012, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards.

KPMG Croatia d.o.o.

KPMG Croatia d.o.o. za reviziju

Croatian Certified Auditors

Eurotower, 17th floor,

Ivana Lučića 2a

10000 Zagreb, Croatia

K P M G Croatia

1 d.o.o.

Eurotower, 17. kat

Ivana Lučića 2a, 10000 Zagreb

8 March 2013

This version of our audit report is a translation from the original, which was prepared in the 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.

MEDIKA d.d.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER 2012

<i>(all amounts are expressed in thousands of HRK)</i>	Note	2012	2011
Revenues	5, 6	2,244,484	2,172,355
Cost of trade goods sold	6	(1,993,901)	(1,929,262)
Staff costs	7	(102,718)	(99,399)
Marketing and promotion expenses	8	(7,339)	(10,350)
Depreciation and amortisation	14, 15	(16,206)	(17,774)
Other operating expenses	9	(62,762)	(60,024)
Other gains / (loss) – net	10	6,009	(7,166)
Operating profit		67,567	48,380
Finance costs – net	11	(16,579)	(23,962)
Share of profits in associates	16	623	783
Profit before tax		51,611	25,201
Income tax	12	(3,341)	(6,810)
Profit for the year		48,270	18,391
Other comprehensive income		-	-
Total comprehensive income		48,270	18,391
Earnings per share:			
- basic/diluted (<i>in HRK</i>)	13	1,687.47	626.55

The consolidated financial statements set out on pages 6 to 49 were approved by the Management Board of the Company in Zagreb on 8 March 2013.

Jasminko Herceg
Member of the Management Board

Medika d.d.
Z A G R E B, Capraška

The accompanying notes on pages 11 to 49 form an integral part of these consolidated financial statements.

MEDIKA d.d.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2012

<i>(all amounts are expressed in thousands of HRK)</i>	Note	As at 31 December	
		2012	2011
ASSETS			
Non-current assets			
Property and equipment	14	159,679	166,756
Intangible assets	15	190,019	175,082
Investment in associates	16	39,182	17,709
Deferred tax asset	27	1,031	2,666
Trade and other receivables	18	16,479	792
		<u>406,390</u>	<u>363,005</u>
Current assets			
Inventories	19	216,553	213,788
Trade and other receivables	18	1,371,586	1,240,809
Income tax receivable		3,784	2,028
Cash and cash equivalents	20	19,566	40,579
		<u>1,611,489</u>	<u>1,497,204</u>
Total assets		2,017,879	1,860,209
EQUITY AND LIABILITIES			
Capital and reserves			
Share capital	21	37,439	37,848
Reserve for reinvested profit	22	33,817	-
Reserves	23	67,278	67,278
Retained earnings	24	236,772	222,319
		<u>375,306</u>	<u>327,445</u>
Non-current liabilities			
Borrowings	26	136,977	36,421
Deferred tax liability	27	15,342	15,134
Provisions	28	679	598
		<u>152,998</u>	<u>52,153</u>
Current liabilities			
Trade and other payables	25	1,293,518	1,119,807
Income tax liabilities		485	151
Borrowings	26	194,097	359,179
Provisions	28	1,475	1,474
		<u>1,489,575</u>	<u>1,480,611</u>
Total equity and liabilities		2,017,879	1,860,209

The accompanying notes on pages 11 to 49 form an integral part of these consolidated financial statements.

MEDIKA d.d.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2012

<i>(all amounts are expressed in thousands of HRK)</i>	Note	Share capital	Reserve for reinvested profit	Reserves	Retained earnings	Total
As at 1 January 2011		43,879	-	62,730	208,770	315,379
Total comprehensive income						
Profit for the year		-	-	-	18,391	18,391
Other comprehensive income		-	-	-	-	-
Total comprehensive income		-	-	-	18,391	18,391
Transactions with owners recognized directly in equity						
Release of treasury shares	21	1,995	-	-	-	1,995
Acquisition of own shares	21	(8,026)	-	-	-	(8,026)
Payment of dividends	24	-	-	-	(294)	(294)
Transfer	23	-	-	4,548	(4,548)	-
Transactions with owners recognized directly in equity		(6,031)	-	4,548	(4,842)	(6,325)
As at 31 December 2011		37,848	-	67,278	222,319	327,445
As at 1 January 2012		37,848	-	67,278	222,319	327,445
Total comprehensive income						
Profit for the year		-	-	-	48,270	48,270
Other comprehensive income		-	-	-	-	-
Total comprehensive income		-	-	-	48,270	48,270
Transactions with owners recognized directly in equity						
Transfer	22	-	33,817	-	(33,817)	-
Release of treasury shares	21	1,815	-	-	-	1,815
Acquisition of own shares	21	(2,224)	-	-	-	(2,224)
Transactions with owners recognized directly in equity		(409)	33,817	-	(33,817)	(409)
As at 31 December 2012		37,439	33,817	67,278	236,772	375,306

The accompanying notes on pages 11 to 49 form an integral part of these consolidated financial statements.

MEDIKA d.d.**CONSOLIDATED STATEMENT OF CASH FLOW****FOR THE YEAR ENDED 31 DECEMBER 2012**

<i>(all amounts expressed in thousands of HRK)</i>	Note	2012	2011
Profit for the year		48,270	18,391
Adjustments for:			
Income tax	12	3,341	6,810
Depreciation and amortisation	14, 15	16,206	17,774
Impairment of receivables	9	5,771	3,679
Inventory impairment	19	4,317	3,979
Unrealised foreign exchange differences		(1,809)	3,830
Change in provisions	28	82	(739)
Gains on sale of tangible assets	10	(600)	(434)
Impairment of property and equipment	9, 14	240	-
Impairment of intangible assets	15	-	6
Interest income		(569)	(409)
Interest expense	11	18,069	18,809
Expenses from bills of exchange discount	11	-	1,504
Share of (profit) / loss from associates	16	(623)	(783)
Gain on disposal of subsidiary	10	(7,470)	-
Changes in:			
Inventories		(5,659)	27,101
Trade and other receivables		(170,406)	(155,885)
Trade and other payables		166,356	63,755
Cash generated from operating activities		75,516	7,388
Interest paid		(19,344)	(18,881)
Income tax paid		(5,005)	(9,843)
Cash flows from operating activities		51,167	(21,336)
Cash flows from investing activities			
Purchase of property and equipment	14	(9,738)	(3,404)
Proceeds from sale of property and equipment		1,264	581
Purchase of intangible assets	15	(14,599)	(1,478)
Acquisition of subsidiary, net of cash acquired	31	(5,888)	(38,722)
The effect of disposal of subsidiary	32	(172)	-
Proceeds from the repayment of loans given		4,284	5,412
Loans given		(9,803)	(1,588)
Interest received		569	409
Cash paid for shares in subsidiaries	16	(450)	-
Dividend received	16	748	341
Cash flows from investing activities		(33,785)	(38,449)

The accompanying notes on pages 11 to 49 form an integral part of these consolidated financial statements.

MEDIKA d.d.

CONSOLIDATED STATEMENT OF CASH FLOW (continued)

FOR THE YEAR ENDED 31 DECEMBER 2012

<i>(all amounts expressed in thousands of HRK)</i>	Note	2012	2011
Cash flows from financing activities			
Repayment of borrowings		(313,138)	(164,819)
Proceeds from borrowings		279,198	244,896
Repayment of finance lease		(2,231)	(2,574)
Acquisition of own shares	21	(2,224)	(8,026)
Dividend payment		-	(378)
Cash flows from financing activities		(38,395)	69,099
Net (decrease) / increase in cash and cash equivalents		(21,013)	9,314
Cash and cash equivalents at beginning of year		40,579	31,265
Cash and cash equivalents at end of year	20	19,566	40,579

The accompanying notes on pages 11 to 49 form an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 1 – GENERAL INFORMATION

Medika d.d. (hereinafter: “the Company”) is a joint stock company incorporated in Croatia. The principal activity of the Company and its subsidiaries (together “the Group”) is the wholesale and retail distribution of pharmaceutical products. The Company headquarters is in Zagreb, Capraška 1.

The Group is comprised of the Company and the following subsidiaries and associates:

	<u>2012</u>	<u>2011</u>
- Zdravstvena ustanova Ljekarne Prima Pharme, Split	100%	100%
- Zdravstvena ustanova Ljekarne Delonga, Okrug Gornji (from May 2007)	100%	100%
- Zdravstvena ustanova Ljekarne Ines Škoko, Zagreb (from March 2011)	100%	100%
- Ljekarna Dragica Blagus-Vičanović, Strahoninec (from May 2011)	-	100%
- Zdravstvena ustanova Ljekarne Atalić, Osijek (from June 2011)	100%	100%
- Ljekarna Alagić, Split (from August 2012)	100%	-
- Zdravstvena ustanova Ljekarne Čaić, Bošnjaci (from October 2012)	100%	-
- Zdravstvena ustanova Ljekarne Jagatić, Zagreb (from November 2008)	49%	49%
- Primus nekretnine d.o.o., Zagreb (established in 2009)	-	100%
- Litmus d.o.o., Zagreb (established in August 2012)	41.53%	-

As at 31 December 2012, the Company’s shares were listed on the official market on the Zagreb Stock Exchange. The shareholder structure is shown in note 21.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

2.1 Basis of preparation

Consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS). Consolidated financial statements have been prepared under the historical cost convention, unless otherwise stated.

These financial statements are a translation of the official statutory financial statements prepared in Croatian.

The preparation of consolidated financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group’s accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in note 4.

New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations have been released and are not yet effective for the year ended 31 December 2012, and have not been applied in preparing these financial statements. None of these are expected to have a significant effect on the financial statements of the Group.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.2 Consolidation

(a) Subsidiaries

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

The purchase method of accounting is used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill (note 2.6). If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

Inter-group transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated, but considered if an impairment indicator of the asset transferred exists. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

(b) Associates

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Group holds between 20 and 50 percent of the voting power of another entity. In Group's financial statements, these investments are stated using expense method.

The Group's share of its associates' post-acquisition profits or losses is recognized in the income statement, and its share of post-acquisition movements in reserves is recognized in reserves. The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivable which form an integral part of net investments, the Group does not recognize further losses, unless it has incurred obligations or made payments on behalf of the associate.

Unrealized gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealized losses are also eliminated, unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

2.3 Segment reporting

A business segment is an integral part of the business entity that engages in business activities from which revenues can be realized, by which costs are incurred and for which there are separate financial information. Its operating results are regularly reviewed and evaluated by chief operating decision maker of the business entity in order to decide on resources to be allocated to the segment.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.4 Foreign currencies

(a) Functional and presentation currency

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

(b) Transactions and balances in foreign currencies

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

Non-monetary assets and items that are measured at foreign currency historical cost are not retranslated at new exchange rates.

Non-monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated into functional currency at foreign exchange rates ruling at the dates at which the values were determined.

2.5 Property and equipment

Property and equipment is included in the statement of financial position at historical cost less accumulated depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of property and equipment.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Land and assets under construction are not depreciated. Depreciation of other assets is calculated using the straight-line method to allocate their cost over their estimated useful lives. Depreciation is calculated for each asset until the asset is fully depreciated or to its residual values if significant.

The estimated useful lives are as follows:

Buildings	10-40 years
Equipment	2-20 years

The residual value of an asset is the estimated amount that the Group would currently obtain from disposal of the asset less the estimated costs of disposal, if the asset was already of the age and in the condition expected at the end of its useful life. The residual value of an asset is nil if the Group expects to use the asset until the end of its physical life. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.5 Property and equipment (continued)

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 (note 2.7).

Gains and losses on disposals are determined by comparing the proceeds with carrying amount, and are recognised within 'other gains – net' in the income statement.

2.6 Intangible assets

(a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net identifiable assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisition of subsidiaries is included in intangible assets.

Separately recognised goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units that are expected to benefit from the business combination in which the goodwill arose. The Group allocates goodwill to each business segment in which it operates.

Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

(b) Licences

Acquired pharmaceutical service licences are capitalised by the amount for which future economic benefits are expected. These licences are amortized over their estimated useful life of 5 to an infinite lifetime. Recoverable amount is estimated on an annual basis.

(c) Software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised over their estimated useful lives (5 to 10 years).

(d) Other rights

Other rights are shown at historical cost, they have a finite useful life and are carried at cost less accumulated amortisation. Amortisation is calculated using the straight-line method to allocate the cost of other rights over their estimated useful lives (5 years).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.7 Impairment of non-financial assets

Assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

2.8 Financial assets

The Group classifies its financial assets as trade and other receivables. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

Trade and other receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are included in current assets, except for maturities greater than 12 months after the reporting date. These are classified as non-current assets.

Trade and other receivables are measured at amortised cost using effective interest rate method.

The Group assesses at each reporting date whether there is indication for financial asset or a group of financial assets to be impaired. Impairment testing of given loans and receivables is described in note 2.11.

2.9 Leases

The Group leases certain property and equipment. Leases of property, plant and equipment, where the Group has substantially all the risks and rewards of ownership, are classified as finance leases. Finance leases are capitalized at the inception of the lease at the lower of fair value of the leased property or the present value of minimum lease payments. Each lease payment is allocated between the liability and finance charges so as to achieve a constant rate on the balance outstanding. The interest element of the finance costs is charged to the income statement over the lease period. The property, plant and equipment acquired under finance leases are depreciated over the shorter of the useful life or the lease term.

Leases where the significant portion of risks and rewards of ownership are not transferred to the Group are classified as operating leases. Payments made under operating leases are charged to the income statement on a straight-line basis over the period of the lease.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.10 Inventories

Inventories are stated at the lower of cost or net realisable value. Cost includes all costs attributable to the purchase of goods and is calculated based on the average purchase price. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses. At each reporting date, the Group examines if there are damaged and/or expired inventories. With respect to differences identified, a provision is made for such inventories against cost of trade goods sold.

2.11 Trade and loan receivables

Trade and loan receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables.

Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy, and default or delinquency in payments are considered indicators that the receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The amount of the provision is recognised in the income statement within 'other operating expenses'.

Loans and receivables with maturities greater than 12 months after the reporting date are classified as non-current assets.

2.12 Cash and cash equivalents

Cash and cash equivalents comprise cash in hand, deposits held at call with banks and other short-term highly liquid instruments with original maturities of three months or less.

2.13 Share capital

Ordinary shares are classified as equity.

When the Company purchases its 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, reissued or disposed of. Where such shares are subsequently sold or 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.

2.14 Trade payables

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.15 Borrowings

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

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

2.16 Income tax

The current income tax charge is calculated on the basis of the tax law enacted at the reporting date in Croatia. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulations are subject to interpretation and consider establishing provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred tax asset and liability are determined using tax rates (and laws) that have been enacted or substantially enacted by the reporting date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

2.17 Employee benefits

(a) Pension obligations and post-employment benefits

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

(b) Long-term employee benefits

The Group recognises a liability for long-term employee benefits (jubilee awards and termination benefits as defined by the collective bargaining agreement) evenly over the period the jubilee award/termination benefit is earned based on actual years of service. The long-term employee benefit liability includes assumptions regarding the likely number of staff to whom the benefit will be payable, estimated benefit cost and the discount rate. Termination benefits and jubilee awards falling due more than 12 months after the reporting date are discounted to their present value.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.17 Employee benefits (continued)

(c) Short-term employee benefits

The Group recognises a provision for bonuses, unused annual leave and other considerations where contractually obliged or where there is a past practice that has created a constructive obligation.

Short-term liabilities for termination benefits are payable when employment is terminated by the Group before the normal retirement date, or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognises termination benefits when it is demonstrably committed to either: terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal; or providing termination benefits as a result of an offer made to encourage voluntary redundancy.

Short-term employee benefits include termination benefits and jubilee awards (stated in paragraph (b) previously mentioned), which will be paid within a period of 12 months after the reporting date.

2.18 Provisions

Provisions for costs are recognised when: the Group has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated.

When there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The amount of provision increases in each period to reflect the passage of time. This increase is shown as interest expense.

2.19 Revenue recognition

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

The Group recognises revenue when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity and specific criteria have been met for each of the Group's activities as described below.

(a) Sale of goods

Income from the wholesale of goods is recognised when the Group has delivered products to the customer, the customer has accepted the products and collectability of the related receivables is reasonably assured. Products are sold with volume discounts and customers have a right to return faulty products in the wholesale market. Sales are recorded based on the price specified in the sales contracts, net of estimated volume discounts and returns at the time of sale.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.19 Revenue recognition (continued)

(a) Sale of goods (continued)

Income from the retail sales of goods is recognised when the Group sells a product to the customer. Retail sales are usually in cash or by credit card. The recorded revenue includes credit card fees payable for the transaction. Such fees are included in other operating expenses.

(b) Sale of services

Service revenue mainly relates to revenue from consignment commissions and is recognised when the goods are taken from the consignment warehouse and when a calculation of the consignment service provided is prepared for the owner of the goods.

(c) Interest income

Interest income arising from fixed-term bank deposits and given loans is recognised on a time-proportion basis using the effective interest method.

2.20 Finance expenses

Finance expenses comprise interest expense on borrowings, changes in the fair value of financial assets at fair value through profit or loss, impairment losses recognised on financial assets and foreign currency losses. All borrowing costs are recognised in profit or loss using the effective interest method.

2.21 Dividend distribution

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

2.22 Value added tax

The Tax Authorities require the settlement of VAT on a net basis. VAT related to sales and purchases is recognised and disclosed in the statement of financial position on a net basis. Where a provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

2.23 Earnings per share

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 3 – FINANCIAL RISK MANAGEMENT

3.1 Financial risk factors

The Group's activities expose it to a variety of financial risks: market risk (including currency risk, fair value interest rate risk, cash flow interest rate risk and equity securities risk) credit risk and liquidity risk. The Group does not have a written risk management programme, and did not use derivative financial instruments to actively hedge financial risks. However, overall risk management in respect of these risks is carried out by the Group's Finance department.

(a) Market risk

(i) Foreign exchange risk

The Group's sales are predominantly realised on the domestic market in Croatian kuna (HRK). However, the Group's purchase of goods is predominantly realised on the foreign market. Furthermore, a part of the borrowings is linked to foreign currencies. The Group is therefore exposed to foreign exchange risk arising from various changes in foreign exchange rates mainly linked to the EUR, which may have an impact on future operating results and cash flows.

As at 31 December 2012, if the EURO had weakened/strengthened against the HRK by 1.56% (2011: 1.35%), with all other variables held constant, the profit after tax for the reporting period would have been HRK 5,311 thousand higher/lower (2011: HRK 5,889 thousand), mainly as a result of foreign exchange gains/losses on translation of EURO-denominated trade payables and liabilities and loans and borrowings.

(ii) Cash flow and fair value interest rate risk

As the Group has no significant interest-bearing assets, the Group's income and operating cash flows are substantially independent of changes in market interest rates.

The Group's interest rate risk arises from issued bonds and commercial bills and long-term borrowings. Borrowings issued at variable rates expose the Group to cash flow interest rate risk. Borrowings issued at fixed rates expose the Group to fair value interest rate risk.

The Group does not use derivative instruments to actively hedge cash flow and fair value interest rate risk exposure. However, the Group continuously monitors changes in interest rates. Various scenarios are simulated taking into account refinancing, renewal of existing positions and alternative financing.

As at 31 December 2012, if the effective interest rate on borrowings (issued at variable rate) had been 1.56% higher/lower on an annual level (2011: 1.32%), the profit after tax for the reporting period would have been HRK 3,032 thousand lower/higher by HRK thousand (2011: HRK 3,712 thousand).

(iii) Equity securities risk

The Group does not have any equity securities and therefore it is not exposed to this financial risk.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 3 – FINANCIAL RISK MANAGEMENT (continued)

3.1 Financial risk factors (continued)

(b) Credit risk

Group's exposure to credit risk is influenced mainly by current assets which comprise cash, trade and other receivables. The Group does not have a significant concentration of credit risk. Group's sales policies ensure that sale is done towards customers with adequate credit history. As for the credit exposure, customers are divided into three categories: pharmacies, hospitals and other customers. Pharmacies present higher credit risk since they have potential going concern issue. On the other hand, collection period for hospitals is longer, but there are no impairment indications, namely, there is no going concern issue. The majority of receivables are either financially dependent or owned by the State causing the Group, from perspective of credit risk exposure, also to be dependent on the State. Other customers are not significant because of dispersion on large number of customers, individually small balances and Group's strict measures of collection of outstanding debts and delivery of goods. The Group insures part of the trade receivables by bills of exchange and promissory notes. Detailed credit risk analysis is shown under notes 17 and 18.

(c) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash, the availability of funding through an adequate amount of committed credit facilities and the ability to meet all obligations. The Group aims to maintain flexibility in funding by keeping committed credit lines available. The Finance department regularly – monthly monitors available cash resources. The Commission in charge of monitoring the Group's liquidity prepares a payment plan on a monthly basis, and makes decisions on a daily basis with respect to payments, in accordance with the priority list received from managers who are in charge of the purchase of specific groups of products. The majority of debtors are either financially dependent or owned by the State so the Group is also dependent on the State on the liquidity risk side.

The table below analyses financial liabilities of the Group according to contracted maturities. The amounts stated below represent undiscounted cash flows.

<i>(in thousands of HRK)</i>	Less than 1 year	Between 1-3 years	Over 3 years	Total
31 December 2012				
Trade and other payables	1,293,518	-	-	1,293,518
Borrowings	212,594	36,168	111,956	360,718
 <i>(in thousands of HRK)</i>				
31 December 2011				
Trade and other payables	1,119,807	-	-	1,119,807
Borrowings	371,099	36,165	-	407,264

During 2013, the Group will settle trade and other liabilities according to the collection of receivables which depends on liquidity of the whole healthcare system.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 3 – FINANCIAL RISK MANAGEMENT (continued)

3.2 Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt.

The Group monitors its capital using gearing ratios in consolidated financial statements, according to the covenants relevant to issued bonds.

The Group monitors its capital using gearing ratios, the most significant of which is the self-financing ratio, which should not move below the threshold of 15%. This ratio is calculated as the proportion of total equity and total assets.

The self-financing ratio is as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Total equity (capital and reserves)	375,306	327,445
Total assets	<u>2,017,879</u>	<u>1,860,209</u>
Self-financing ratio	19%	18%

In 2012, the ratio has increased in comparison to 2011 showing that 19% of the Group's total assets are financed from own resources. In accordance with the stated, 81% of assets is financed from other resources.

3.3 Fair value estimation

The fair value of financial instruments traded in active markets is based on quoted market prices at the reporting date. The quoted market price used for financial assets held by the Group is the current bid price. The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. The Group uses a variety of methods and makes assumptions that are based on market conditions existing at each reporting date.

The carrying value less impairment provision of trade receivables and payables are assumed to approximate their fair values.

The fair value of financial liabilities for disclosure purposes is estimated by discounting the future contractual cash flows at the current market interest rate that is available to the Group for similar financial instruments.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 4 – CRITICAL ACCOUNTING ESTIMATES

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

Assumptions to determine amount of provisions of trade receivables

Due to the materiality of the amount of trade receivables recorded in the statement of financial position, Management estimates the likelihood of the collection of trade receivables based on an analysis of such assets. Factors taken into consideration by Management include: ageing analysis of trade receivables and the financial position of customers compared to the collection history with the customer. The estimated recoverable amount of trade receivables represents the present value of estimated future cash flows, discounted at the annual effective interest rate of 4.99 % (2011: 5.73 %). Should actual collections be less than management estimates, the Group would be required to record additional impairment expense.

As at 31 December 2012, if the amount of uncollectible receivables in total receivables past due had been 1% lower/higher, with all other variables held constant, profit after tax for the reporting period would have been HRK 1,327 thousand higher/lower than the one recorded (2011: HRK 1,888 thousand), i.e., the effect in the hospital segment would be HRK 879 thousand (2011: HRK 1,485 thousand), in the pharmacy segment HRK 169 thousand (2011: HRK 112 thousand) and in the segment 'other' HRK 279 thousand (2011: HRK 291 thousand).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 5 - REVENUES

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Revenue from sales	2,229,932	2,161,585
Other revenues	<u>14,552</u>	<u>10,770</u>
	<u>2,244,484</u>	<u>2,172,355</u>

Other revenues include interest income in the amount of HRK 569 thousand (2011: HRK 340 thousand)

NOTE 6 – BUSINESS SEGMENT INFORMATION

Segment information follows the structure used by the Company and the Group for internal reporting purposes, which has remained unchanged in comparison with the previous year.

The Group monitors revenues and gross profit through two main distribution channels: wholesale and retail.

The wholesale distribution channel consists of:

1. Pharmacies, which are for the purpose of reporting, divided into following categories:

- county pharmacies
- private pharmacies

The Group operates with approximately 440 pharmacies and health institutions.

2. Hospitals, which are by the Regulation on conditions for the classification of hospitals (passed as a part of health system reform started in 2011), divided into following categories:

- national hospitals
- county hospitals with regional significance
- county hospitals
- local hospitals

3. Other customers divided into:

- dental practices
- veterinary clinics
- medical centres
- pharmacy wholesalers
- other customers (herbal pharmacies, companies, optics, etc.)

Retail distribution channel consists of self-owned pharmacies (subsidiary ZU Prima Pharme and its subsidiaries).

The Company uses margin calculated as sales revenue minus cost of goods sold as a measure of success of a particular segment.

Transactions between segments do not exist. The Company and The Group apply the same accounting policies for all segments.

Transactions between Group members are measured at market prices.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 6 – BUSINESS SEGMENT INFORMATION (continued)

The results of the stated segments for the year ended 31 December 2012 are as follows:

<i>(in thousands of HRK)</i>	Wholesale			Retail	Total
	Pharmacies	Hospitals	Other	Self-owned pharmacies	
Revenue from sales	1,061,858	526,586	297,104	316,346	2,201,894
Other revenue	-	-	12,160	2,392	14,552
Revenue from sales and other revenue from related parties	27,771	-	267	-	28,038
Total revenues	1,089,629	526,586	309,531	318,738	2,244,484
Cost of trade goods sold	(991,353)	(479,451)	(272,945)	(250,152)	(1,993,901)
Segment results	98,276	47,135	36,586	68,586	250,583
Operating expenses					(183,016)
Operating profit					67,567
Finance costs - net					(16,579)
Share of profits in associates					623
Profit before tax					51,611
Income tax					(3,341)
Profit for the year					48,270

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 6 – BUSINESS SEGMENT INFORMATION (continued)

The results of the stated segments for the year ended 31 December 2011 are as follows:

<i>(in thousands of HRK)</i>	Wholesale			Retail	Total
	Pharmacies	Hospitals	Other	Self-owned pharmacies	
Revenue from sales	1,050,954	533,366	263,944	299,486	2,147,750
Other revenue	-	-	8,530	2,195	10,725
Revenue from sales and other revenue from related parties	13,835	-	45	-	13,880
Total revenues	1,064,789	533,366	272,519	301,681	2,172,355
Cost of trade goods sold	(977,948)	(483,395)	(236,272)	(231,647)	(1,929,262)
Segment results	86,841	49,971	36,247	70,034	243,093
Operating expenses					(194,713)
Operating profit					48,380
Finance costs - net					(23,962)
Share of profits in associates					783
Profit before tax					25,201
Income tax					(6,810)
Profit for the year					18,391

The segment trade receivables at 31 December 2012 are as follows:

<i>(in thousands of HRK)</i>	Wholesale			Retail	Total
	Pharmacies	Hospitals	Other	Self-owned pharmacies	
Trade receivables (note 18 /ii/)	594,816	540,116	83,038	137,179	1,355,149

The segment trade receivables at 31 December 2011 are as follows:

<i>(in thousands of HRK)</i>	Wholesale			Retail	Total
	Pharmacies	Hospitals	Other	Self-owned pharmacies	
Trade receivables (note 18 /ii/)	501,764	538,912	94,354	100,256	1,235,286

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 7 – STAFF COSTS

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Net salaries	53,710	51,097
Tax and surtax	17,671	15,975
Contributions from and on salaries /i/	20,858	21,349
Termination benefits	597	332
Employee transportation costs	3,248	2,875
Other employee benefits /ii/	2,526	3,509
Bonuses	4,108	4,262
	<u>102,718</u>	<u>99,399</u>

As at 31 December 2012, the Group had 724 employees (2011: 697 employees).

/i/ In 2012, pension contributions calculated by the Group for payment to mandatory pension funds amounted to HRK 15,765 thousand (2011: HRK 14,801 thousand).

/ii/ Other employee benefits relate to provision for accrual for unused vacation days, business trip expenses, aids, awards etc.

NOTE 8 – MARKETING AND PROMOTION EXPENSES

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Entertainment	2,144	4,025
Marketing	2,270	1,604
Donations	2,925	4,721
	<u>7,339</u>	<u>10,350</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 9 – OTHER OPERATING EXPENSES

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Impairment of trade receivables (note 18/ii/)	5,771	3,679
Maintenance of assets, security services and insurance	10,810	11,163
Materials and energy consumed	12,741	11,812
Rental expenses	11,259	9,831
Taxes and contributions irrespective of results	3,331	5,956
Professional training and consultancy services	5,016	5,137
Bank charges and payment transaction costs	4,127	3,184
Telephone, postal and utility services	2,625	2,241
Impairment of property and equipment (note 14)	240	-
Other expenses	6,842	7,021
	<u>62,762</u>	<u>60,024</u>

NOTE 10 – OTHER GAINS / (LOSSES) – NET

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Gain on disposal of subsidiary (note 32)	7,470	-
Gains on sale of property and equipment (net)	600	434
Net foreign exchange losses	(2,061)	(7,600)
	<u>6,009</u>	<u>(7,166)</u>

NOTE 11 – FINANCE COSTS - NET

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Interest expense:		
Bank borrowings and finance lease	(18,069)	(18,809)
Bills of exchange expense	-	(1,504)
	<u>(18,069)</u>	<u>(20,313)</u>
Foreign exchange gains / (losses) – net		
Foreign exchange gains	3,694	2,364
Foreign exchange losses	(2,204)	(6,013)
	<u>1,490</u>	<u>(3,649)</u>
	<u>(16,579)</u>	<u>(23,962)</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 12 – INCOME TAX

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Current tax	3,437	6,744
Deferred tax (note 26)	(96)	66
	<u>3,341</u>	<u>6,810</u>

Reconciliation of Group's tax expense as per income statement and legal tax rate is shown below:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Profit before taxation	51,611	25,201
Income tax (20%)	10,322	5,040
Tax exemption for reinvested profit (note 22)	(6,763)	-
Income non assessable and tax incentives	(1,976)	(152)
Expenses not deductible	1,725	1,707
Losses not recognized as deferred tax asset	101	227
Unrecognised losses utilised	-	(12)
Temporary tax differences for which no deferred tax is recognised	(68)	-
Income tax	<u>3,341</u>	<u>6,810</u>
Effective tax rate	<u>6.47%</u>	<u>27.02%</u>

In accordance with local regulations, the Tax Authority may at any time inspect the Group'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 Group's management is not aware of any circumstances, which may give rise to a potential material liability in this respect.

NOTE 13 – EARNINGS PER SHARE

Earnings per share is calculated by dividing the net profit of the Group by the weighted average number of ordinary shares in issue during the year, excluding the average number of ordinary shares purchased by the Company and held as treasury shares. Average number of shares in amount of 28,605 is the result of releasing treasury shares in June 2012 and acquiring treasury shares in July 2012.

	<u>2012</u>	<u>2011</u>
Net profit attributable to shareholders <i>(in thousands of HRK)</i>	48,270	18,391
Weighted average number of ordinary shares excluding treasury shares	28,605	29,353
Basic/diluted earnings per share <i>(in HRK)</i>	<u>1,687.47</u>	<u>626.55</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 14 – PROPERTY AND EQUIPMENT

(all amounts are expressed in thousands of HRK)

	Land	Buildings	Equipment	Assets under construction	Total
As at 31 December 2010					
Cost	16,516	177,085	107,556	3,194	304,351
Accumulated depreciation	-	(45,968)	(85,783)	-	(131,751)
Net book amount	16,516	131,117	21,773	3,194	172,600
For year ended 31 December 2011					
Opening net book amount	16,516	131,117	21,773	3,194	172,600
Additions	-	19	1,822	4,060	5,901
Acquisition of subsidiary (note 31)	-	-	62	-	62
Transfer from assets under construction	-	108	4,384	(4,492)	(147)
Disposals	-	-	(135)	(12)	-
Depreciation	-	(4,277)	(7,383)	-	(11,660)
Closing net book amount	16,516	126,967	20,523	2,750	166,756
As at 31 December 2011					
Cost	16,516	177,212	113,689	2,750	310,167
Accumulated depreciation	-	(50,245)	(93,166)	-	(143,411)
Net book amount	16,516	126,967	20,523	2,750	166,756
For year ended 31 December 2012					
Opening net book amount	16,516	126,967	20,523	2,750	166,756
Additions	-	-	1,096	12,103	13,199
Acquisition of subsidiary (note 31)	-	-	51	-	51
Transfer from assets under construction	-	47	5,667	(5,714)	-
Disposals	-	-	(664)	-	(664)
Impairment	-	(240)	-	-	(240)
Disposal of subsidiary (note 32)	(521)	(8,517)	(17)	-	(9,055)
Depreciation	-	(4,235)	(6,133)	-	(10,368)
Closing net book amount	15,995	114,022	20,523	9,139	159,679
As at 31 December 2012					
Cost	15,995	159,230	96,155	9,139	280,519
Accumulated depreciation	-	(45,208)	(75,632)	-	(120,840)
Net book amount	15,995	114,022	20,523	9,139	159,679

Loans and finance lease liabilities (note 26) have been secured by pledges over tangible fixed assets with a net book value of HRK 135,067 thousand as at 31 December 2012 (2011: HRK 135,152 thousand).

Delivery and personal vehicles under finance lease are as follows:

	2012	2011
	(in thousands of HRK)	
Cost – capitalised finance lease	11,728	10,931
Accumulated depreciation	(5,112)	(5,387)
Net book amount	6,616	5,544

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 15 – INTANGIBLE ASSETS

<i>(all amounts are expressed in thousands of HRK)</i>	Goodwill	Licences, software and other rights	Asset under construction	Total
As at 31 December 2010				
Cost	38,064	125,284	150	163,498
Accumulated amortisation and impairment	-	(29,652)	-	(29,652)
Net book amount	38,064	95,632	150	133,846
For the year ended 31 December 2011				
Opening net book amount	38,064	95,632	150	133,846
Acquisition of subsidiary (note 31)	23,309	22,569	-	45,878
Additions	-	1,316	162	1,478
Transfer	-	193	(193)	-
Disposal	-	(6)	-	(6)
Amortisation	-	(6,114)	-	(6,114)
Closing net book amount	61,373	113,590	119	175,082
At 31 December 2011				
Cost	61,373	149,356	119	210,848
Accumulated amortisation and impairment	-	(35,766)	-	(35,766)
Net book amount	61,373	113,590	119	175,082
For the year ended 31 December 2012				
Opening net book amount	61,373	113,590	119	175,082
Acquisition of subsidiary (note 31)	7,588	1,038	-	8,626
Additions	106	12,329	2,164	14,599
Transfer	-	852	(852)	-
Investment in subsidiary (note 16)	-	(2,450)	-	(2,450)
Amortisation	-	(5,838)	-	(5,838)
Closing net book amount	69,067	119,521	1,431	190,019
At 31 December 2012				
Cost	69,067	161,125	1,431	231,623
Accumulated amortisation and impairment	-	(41,604)	-	(41,604)
Net book amount	69,067	119,521	1,431	190,019

Licences

Licences for performing pharmaceutical services with indefinite useful life at the reporting date amount to HRK 107,021 thousand (2011: HRK 96,714 thousand).

Impairment test of goodwill and licences with indefinite useful life

The Group calculated recoverable amount using value-in-use method. Value-in-use cash flow projections were based on 5 year business plan approved by management. Discount rates of 8.63%, growth rate from 1%-8% and income tax rate of 20% were applied when discounting projected cash flow. Recoverable amount exceeds carrying amount.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 16 – INVESTMENTS IN ASSOCIATES

The Group holds 49% share in the associate Zdravstvena ustanova Ljekarne Jagatić, which was acquired in 2008 and 41.53% share in Litmus d.o.o. which was acquired in 2012.

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
As at 1 January	17,709	17,267
Investment in Litmus d.o.o.	19,148	-
Increase in investment in ZU Ljekarne Jagatić	2,450	-
Receipts from associate	(748)	(341)
Gain / (loss) realized after the acquisition date	<u>623</u>	<u>783</u>
As at 31 December	<u>39,182</u>	<u>17,709</u>

Investment in Litmus d.o.o. arose as a result of the incorporation agreement under which the Company invested its ownership interest in Primus nekretnine d.o.o. into the share capital of Litmus d.o.o. An independent valuer estimated the value investment in Primus nekretnine d.o.o. at HRK 18,698 thousand. In Additionally, the Company made a cash contribution in the amount of HRK 450 thousand, thereby acquiring the total share of 41.53% in Litmus d.o.o. As a result of incorporation Litmus d.o.o., net assets of Primus nekretnine d.o.o. in the amount of HRK 11,228 thousand were disposed of, resulting in realised gain on disposal in the amount of HRK 7,470 thousand (note 10). The effects of the disposal of subsidiary and incorporation the associate are shown in detail in note 32.

An increase in investment in ZU Ljekarne Jagatić was made by contribution of one pharmaceutical licence valued at HRK 2,450 thousand (note 15).

Information on associate company for the year end 31 December can be summarised as follows:

<i>(in thousands of HRK)</i>	<u>Assets</u>	<u>Liabilities</u>	<u>Revenue</u>	<u>Gain / (loss) – net</u>
As at 31 December 2012				
ZU Ljekarne Jagatić	29,802	22,546	44,508	1,549
Litmus d.o.o.	<u>46,050</u>	<u>270</u>	<u>735</u>	<u>(327)</u>
Total	<u>75,852</u>	<u>22,816</u>	<u>45,243</u>	<u>1,222</u>

<i>(in thousands of HRK)</i>	<u>Assets</u>	<u>Liabilities</u>	<u>Revenue</u>	<u>Gain / (loss) – net</u>
As at 31 December 2011				
ZU Ljekarne Jagatić	18,066	16,300	45,216	916
Litmus d.o.o.	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total	<u>18,066</u>	<u>16,300</u>	<u>45,216</u>	<u>916</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 17 – FINANCIAL INSTRUMENTS BY CATEGORY

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Financial assets - category: Loans given and receivables		
Loans given and receivables (note 18/v/)	1,382,866	1,237,034
Cash and cash equivalents (note 20)	19,566	40,579
	<u>1,402,432</u>	<u>1,277,613</u>

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Financial liabilities - category: Other liabilities		
Trade payables (note 25)	1,272,960	1,099,966
Other liabilities (note 25)	20,558	19,841
Total debt (note 26)	331,074	395,600
	<u>1,624,592</u>	<u>1,515,407</u>

The credit quality of financial assets that are neither past due nor impaired can be assessed by reference to historical information about counterparty default rates. The credit quality of financial assets that are neither past due nor impaired is monitored based on the customers' exposure to credit risk:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Hospitals	154,145	210,173
Pharmacies	337,095	164,762
HZZO	135,272	213,449
Other	39,707	39,308
At 31 December	<u>666,219</u>	<u>627,692</u>

MEDIKA d.d.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 18 – TRADE AND OTHER RECEIVABLES

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Non-current receivables:		
Loans given /i/	15,507	792
Long-term deposits	972	-
	<u>16,479</u>	<u>792</u>
Current receivables:		
Trade receivables /ii/	1,355,149	1,235,286
Other current receivables /iii/	4,227	4,567
Loans given /i/,/iv/	7,600	521
Loans given-current maturity of non-current receivables /i/	4,610	435
	<u>1,371,586</u>	<u>1,240,809</u>
	<u>1,388,065</u>	<u>1,241,601</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 18 – TRADE AND OTHER RECEIVABLES (continued)

/i/ Loans given recorded in the statement of financial position as at 31 December are as follows:

	<u>Effective interest rate</u>	<u>2012</u>	<u>2011</u>
		<i>(in thousands of HRK)</i>	
Loans given to pharmacies	4.0%-5.0%	7,468	641
Loans given to others	6.0%	12,649	-
Other		-	586
Total non-current receivables, including current portion		20,117	1,227
Current portion of non-current receivables		(4,610)	(435)
Total non-current receivables		15,507	792

The maturity of long-term loans is as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Between 1 and 2 years	4,135	100
Between 2 and 5 years	11,372	692
	15,507	792

The fair value of long-term loans approximates the carrying amounts since the stated interest rates reflect market rates.

/ii/ Trade receivables recorded in the statement of financial position as at 31 December are as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Domestic trade receivables	1,367,113	1,248,327
Foreign trade receivables	2,353	2,610
Trade receivables – related parties (note 34)	20,130	13,880
	1,389,596	1,264,817
Impairment of trade receivables	(34,447)	(29,531)
	1,355,149	1,235,286

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 18 – TRADE AND OTHER RECEIVABLES (continued)

The ageing structure of receivables past due is as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
0-180 days	540,890	415,166
181-360 days	139,298	97,761
Over 360 days	80,267	124,198
	<u>760,455</u>	<u>637,125</u>

Movements in the provision for impairment of trade receivables are as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
As at 1 January	29,531	26,089
Increase (note 9)	5,771	3,679
Written off	(855)	(237)
As at 31 December	<u>34,447</u>	<u>29,531</u>

The carrying amounts of trade and other receivables are denominated in the following currencies:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
HRK	1,385,880	1,238,703
EUR	2,185	2,898
	<u>1,388,065</u>	<u>1,241,601</u>

/iii/ Other receivables recorded in the statement of financial position as at 31 December are as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
VAT receivable	2,688	2,429
Prepaid expenses	1,060	753
Other	479	1,385
	<u>4,227</u>	<u>4,567</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 18 – TRADE AND OTHER RECEIVABLES (continued)

/iv/ Loans given recorded in the statement of financial position as at 31 December are as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Loans given - other	7,600	1,090
	<u>7,600</u>	<u>1,090</u>
Impairment	-	(569)
	<u>7,600</u>	<u>521</u>

/v/ Financial assets by category include the following:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Cash loans given	12,459	1,748
Commodity loans given	15,258	-
Trade receivables	1,355,149	1,235,286
	<u>1,382,866</u>	<u>1,237,034</u>

Commodity loans given relate to trade receivables due that have been reprogrammed and the payment has been agreed in future periods.

NOTE 19 – INVENTORIES

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Trade goods	199,056	183,385
Trade goods – related parties (note 34)	15,253	27,125
Advances given	1,842	2,878
Office supplies	402	400
	<u>216,553</u>	<u>213,788</u>

Inventories are stated at the lower of cost or net realisable sales value. At each reporting date, damaged and expired inventories are tested. With respect to differences identified, a provision is made for such inventories, which amounted to HRK 4,317 thousand in 2012 (2011: HRK 3,979 thousand) and which is included in cost of trade goods sold.

NOTE 20 – CASH AND CASH EQUIVALENTS

	<u>2012</u>	<u>2010</u>
	<i>(in thousands of HRK)</i>	
Current account	19,405	40,458
Foreign currency account	127	53
Cash in hand and cheques	34	68
	<u>19,566</u>	<u>40,579</u>

Cash on HRK and foreign currency accounts are held with business banks in Croatia. Cash includes cheques with maturity less than three months.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 21 – SHARE CAPITAL

As at 31 December 2011, Company's share capital amounts to HRK 60,388,000, and it is distributed among 30,194 shares. The nominal value per share is HRK 2,000. All issued shares are fully paid.

	Number of shares <i>(in number of shares)</i>	Share capital	Treasury shares <i>(in thousands of HRK)</i>	Capital profit / (loss)	Total
As at 1 January 2011	30,194	60,388	(12,250)	(4,259)	43,879
Release of treasury shares	-	-	4,600	(2,605)	1,995
Acquisition of treasury shares	-	-	(8,026)	-	(8,026)
As at 31 December 2011	30,194	60,388	(15,676)	(6,864)	37,848
As at 1 January 2012	30,194	60,388	(15,676)	(6,864)	37,848
Release of treasury shares \i\	-	-	2,494	(679)	1,815
Acquisition of treasury shares \ii\	-	-	(2,224)	-	(2,224)
As at 31 December 2012	30,194	60,388	(15,406)	(7,543)	37,439

\i\ During 2012, the Company granted 252 of its treasury shares (2011: 285 treasury shares) to key management.

\ii\ During 2012, the Company redeemed a total of 308 of its treasury shares (2011: 1,100 treasury shares).

The ownership structure of the Company is as follows:

	2012		2011	
	Number of shares	%	Number of shares	%
Mavota d.o.o.	14,306	47.38%	14,306	47.38%
Pliva Hrvatska d.o.o.	7,646	25.32%	7,646	25.32%
Krka d.d. Novo Mesto	3,614	11.97%	3,614	11.97%
Treasury shares	1,640	5.43%	1,584	5.25%
Domestic natural persons	1,553	5.14%	1,575	5.22%
Other businesses	1,435	4.76%	1,469	4.86%
Total	30,194	100%	30,194	100%

As at 31 December 2012 Mavota d.o.o. owned 14,306 shares, which represents 50.1% of shares with voting rights taking into account non-voting treasury shares.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 22 – RESERVE FOR REINVESTED PROFIT

During 2012 the Company realised profit before tax of HRK 36,469 thousand. The Management of the Company adopted a decision to reinvest profits for the purpose of long-term goals of encouraging investment in the amount of HRK 33,817 thousand, which will be registered during 2013 as an increase of the Company's share capital. Increase of share capital will be carried out by increasing the nominal value of the shares, which means that existing shareholder rights will not change, and will belong to the shareholders in proportion to their previous participation in the share capital.

In accordance with the applicable tax regulations, the Company recognised the amount of reinvested profit amount as a tax incentive resulting in a decrease in current tax expense in the amount of HRK 6,763 thousand.

It should be noted that the decision to reinvest profits and consequent increase of share capital is subject to final approval by the General Assembly.

The Management of the Company believes it is certain that the above stated increase in share capital from reinvested profits will be approved by the General Assembly due to the approval of the Supervisory Board on 11 December 2012.

Pursuant to the above, HRK 33,817 thousand relates to the amount of profit that will be reinvested and registered as an increase in the Company's share capital and as such is not considered distributable to the shareholders and is disclosed as a 'reserve for reinvested profit'. If the share capital increase is not registered by 31 October 2013, which is period of six months from the expiry of the deadline for filing income tax returns defined by tax authorities, in which the Company must submit proof of the implementation of the share capital increase in the amount of reinvested profit, the tax incentive will be reversed, resulting in a tax expense of HRK 6,763 thousand, plus interests.

NOTE 23 – RESERVES

<i>(in thousands of HRK)</i>	Legal reserves	Reserves for treasury shares	Total
As at 31 December 2010	2,730	60,000	62,730
Changes during the year	4,548	-	4,548
As at 31 December 2011	7,278	60,000	67,278
Changes during the year	-	-	-
As at 31 December 2012	7,278	60,000	67,278

Legal reserves amount to HRK 7,278 thousand. The legal reserve is required under Croatian law according to which the Company, as a Group member, is committed to build up legal reserves to a minimum of 5% of the profit for the year until the legal together with share premium reserve reach 5% of the share capital. Revaluation and legal reserves are not distributable.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 24 – RETAINED EARNINGS

Other reserves in the amount of HRK 31,796 thousand (2011: HRK 31,796 thousand) form part of retained earnings.

In July 2011, the Company paid out the dividend for 2010 in accordance with the decision of the General Assembly. The dividend per share was HRK 10.00.

NOTE 25 – TRADE AND OTHER PAYABLES

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Trade payables /i/	1,272,960	1,099,966
Other payables /ii/	20,558	19,841
	<u>1,293,518</u>	<u>1,119,807</u>

/i/ Trade payables recorded as at 31 December are as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Trade payables – domestic	564,125	492,443
Trade payables – foreign	543,519	478,510
Due to related parties (note 34)	165,316	129,013
	<u>1,272,960</u>	<u>1,099,966</u>

The carrying amounts of trade payables are denominated in the following currencies:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
HRK	850,408	720,022
EUR	408,976	372,010
DKK	13,417	7,868
Other currencies	159	66
	<u>1,272,960</u>	<u>1,099,966</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

/ii/ Other payables recorded as at 31 December are as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Salaries to employees	9,303	8,643
Liabilities for the purchase of new subsidiaries (note 31)	3,640	2,610
Unused vacation days	1,947	2,413
Other taxes and contributions	54	238
VAT payable	1,263	1,955
Dividend payable	1	1
Other	4,350	3,981
	<u>20,558</u>	<u>19,841</u>

NOTE 26 – BORROWINGS

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Long-term borrowings:		
Loans/i/	132,968	32,891
Finance lease /iii/	4,009	3,530
	<u>136,977</u>	<u>36,421</u>
Short-term borrowings:		
Loans/ii/	191,275	357,056
Finance lease /iii/	2,822	2,123
	<u>194,097</u>	<u>359,179</u>
Total borrowings	<u>331,074</u>	<u>395,600</u>

/i/ Long-term loans relate to financing from various banks for the purpose of maintaining an adequate level of working capital. Long-term loans consist of four loans denominated in EUR with a variable interest rate and a maturity of 2 – 6 years and one loan denominated in Croatian kuna (HRK) with a maturity of three years.

/ii/ Short-term loans relate to financing from various banks for the purpose of maintaining an adequate level of working capital. Some of them are denominated in Croatian kuna (HRK), while some of them are denominated in EUR. Some of them bear fixed interest rates. Loans have maturity ranging from three months to one year.

/iii/ Long-term finance lease liabilities relate to the purchase of delivery and personal vehicles. Leases in 2012 were agreed at interest rate of 4.00% (2011: 4.45% to 4.48%). The lease liabilities are repayable within four and five years and they are secured by a pledge over all cars which are subject to the finance lease (note 14). Lease liabilities are effectively secured since the lessor has the right to take over the subject of the lease if the Company stops paying of the liabilities.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2012**

NOTE 26 – BORROWINGS (continued)

The gross finance lease liability is as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Up to one year	3,070	2,366
Between 1 and 5 years	4,260	3,697
Future financing costs	(499)	(410)
Net book value of finance lease liability	<u>6,831</u>	<u>5,653</u>

The net book value of finance lease liability is as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Up to one year	2,822	2,123
Between 1 and 5 years	4,009	3,530
	<u>6,831</u>	<u>5,653</u>

The maturity of long-term borrowings is as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Between 1 and 2 years	25,251	21,064
Between 2 and 5 years	111,373	15,357
Over 5 years	353	-
	<u>136,977</u>	<u>36,421</u>

The effective interest rates at the reporting date are as follows:

	<u>2012</u>		<u>2011</u>	
	<u>HRK</u>	<u>EUR</u>	<u>HRK</u>	<u>EUR</u>
	%	%	%	%
Long-term borrowings				
Loans	5.32%	4.47%-7.32%	3.80%-7.75%	5.67%
Finance lease	-	4.10%-7.73%	-	4.67%-7.88%
Short-term borrowings				
Loans	3.93%-5.92%		4.95%-7.55%	4.85%-5.87%

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 26 – BORROWINGS (continued)

The exposure of the borrowings to interest rate changes and the contractual repricing dates at the reporting date are as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Up to 3 months	-	-
3 - 12 months	198,340	385,960
1 - 3 years	132,734	9,640
	<u>331,074</u>	<u>395,600</u>

Borrowing in the amount of HRK 132,734 thousand is shown and is repayable within a period 1-3 years. As the loan's interest rate is fixed, there is no exposure to interest rate changes, and the loan has a maturity of 1 to 2 years.

The carrying amount of short-term borrowings approximates their fair value.

The carrying amount of the Group's borrowings was translated from the following currencies:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
HRK	299,606	204,301
EUR	31,468	191,299
	<u>331,074</u>	<u>395,600</u>

Loans received are secured by mortgages over Group's buildings (note 14), inventories (note 19), bills of exchange and promissory notes.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 27 – DEFERRED INCOME TAX

Deferred tax asset and the deferred tax liability are measured at the actual tax rate of 20% in accordance with income tax regulations.

Deferred tax asset

<i>(in thousands of HRK)</i>	Inventory impairment	Provision for employee benefits	Transfer of property in the Group	Total
As at 1 January 2011	813	133	1,786	2,732
Tax charged to the income statement	(48)	-	(39)	(87)
Tax credited to the income statement	-	21	-	21
As at 31 December 2011	765	154	1,747	2,666
As at 1 January 2012	765	154	1,747	2,666
Tax charged to the income statement	-	-	(12)	(12)
Tax credited to the income statement	86	22	-	108
Tax at disposal of subsidiary	-	-	(1,731)	(1,731)
As at 31 December 2012	851	176	4	1,031

Deferred tax liability

<i>(in thousands of HRK)</i>	Acquisition of subsidiary - licences
As at 1 January 2011	10,650
Tax arising on acquisition of subsidiary	4,484
As at 31 December 2011	15,134
As at 1 January 2012	15,134
Tax arising on acquisition of subsidiary	208
As at 31 December 2012	15,342

The deferred tax liability arose at the acquisition of the subsidiary as a result of the temporary difference arising from the measurement of assets and liabilities of subsidiaries in consolidation at fair values, while the tax base of assets and liabilities remained at the level of expense. The resulting deferred tax liability affected the increase in goodwill (note 15).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 28 – PROVISIONS

<i>(in thousands of HRK)</i>	<u>Provision for employee benefits</u>	<u>Legal disputes</u>	<u>Total</u>
As at 31 December 2011	774	1,298	2,072
Non-current	598	-	598
Current	176	1,298	1,474
As at 1 January 2012	774	1,298	2,072
Additional provisions	598	-	598
Used during the year	(180)	(336)	(516)
As at 31 December 2012	1,192	962	2,154
Non-current	679	-	679
Current	513	962	1,475

Employee benefits

This provision comprises estimated long-term employee benefits relating to termination benefits and jubilee awards, as defined by the collective bargaining agreement. The non-current portion of the provision relates to estimated acquired rights to termination benefits and jubilee awards that will be paid when one year after the reporting date has expired. The current portion of employee benefits includes jubilee awards and termination benefits which will be paid within 12 months after the reporting date.

Legal disputes

During 2012, the Group released provision for one legal dispute which ended in plaintiff's favour. On the basis of lawyer's and Management's estimation of probability of losing the dispute, the Group has not made additional provisions. During 2012, there were no additional legal disputes.

NOTE 29 – COMMITMENTS

The Company entered into several legal disputes, both as plaintiff and defendant. Based on the opinion of the expert legal counsellor who represents the Company in the stated disputes, Management estimates that no material losses shall arise from these disputes for the Company except for two disputes for which provision was made in amount of HRK 962 thousand (note 28).

NOTE 30 – OPERATING LEASE

The Group rents vehicles and office space under non-cancellable operating lease contracts. Lease periods are between 1 and 6 years.

Contractual rents on operating lease are as follows:

	<u>2012</u>	<u>2011</u>
	<i>(in thousands of HRK)</i>	
Up to one year	7,720	7,002
Between 1 and 5 years	23,708	19,591
Over 5 years	12,751	9,790
Contractual rents on operating lease	44,179	36,383

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 31 – ACQUISITION OF SUBSIDIARIES

Acquisition of Health Institutions

In 2012, the Group acquired 100% ownership over one health institutions and one pharmacy (2011: two health institutions and one pharmacy) for an amount of HRK 9,944 thousand (2011: HRK 41,889 thousand).

From the date of acquisition to the reporting date, the Company generated revenues on the basis of newly acquired subsidiaries in the amount of HRK 1,075 thousand (2011.: HRK 8,294 thousand) and profit in the amount of HRK 42 thousand (2011.: HRK 826 thousand).

If the acquisition had occurred on 1 January, estimated revenue for the year ended 31 December 2012 would have been HRK 12,263 thousand higher (2011: HRK 96 thousand higher), while profit before taxation would have been HRK 1,384 thousand higher (2011: HRK 120 thousand higher) than stated. These amounts have been calculated using the Group's accounting policies. Details of the net book value of assets acquired and goodwill determined are as follows:

	31 December 2012	31 December 2011
	<i>(in thousands of HRK)</i>	
Purchase consideration	9,944	41,889
- Cash paid	6,304	39,279
- Liabilities for the purchase of subsidiaries	3,640	2,610
Fair value of assets acquired	(2,356)	(18,580)
Goodwill (note 15)	7,588	23,309

Fair value of acquired asset is as follows:

	2012	2011
	<i>(in thousands of HRK)</i>	
Intangible assets (note 15)	1,038	22,569
Property and equipment (note 14)	51	62
Inventory	1,423	1,638
Loans given	2,197	-
Trade receivables	4,895	9,417
Cash and cash equivalents	416	557
Deferred tax liability (note 27)	(208)	(4,484)
Non-current liabilities	(1,089)	-
Current liabilities	(6,367)	(11,179)
Net assets acquired	2,356	18,580
Purchase consideration paid in cash	6,304	39,279
Cash and cash equivalents acquired	(416)	(557)
Cash used in the acquisition	5,888	38,722

The Group has allocated the purchase price on identified assets, including intangible asset which was not identified in the statement of financial position in accordance with IAS 38 *Intangible assets*.

The management of the Group identified and fair valued a pharmacy licence as the only form of intangible assets which arises during the acquisition of medical institutions/ pharmacies. The assets were fair valued at the acquisition date using net current value of cash flows from use of identified, tangible and intangible assets of the Group that can be directly attributed to them.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 32 – DISPOSAL OF SUBSIDIARY AND INCORPORATION OF ASSOCIATE

In accordance with the incorporation agreement of Litmus d.o.o., the Company invested its ownership interest in Primus nekretnine d.o.o. as shown below. An independent valuer estimated the value of Medika's share at HRK 18,698 thousand. As a result of the transaction, the Group realised a gain of HRK 7,470 thousand.

(in thousands of HRK)

Operating result of the subsidiary

	<u>2012</u>
Revenue	-
Expenses	(429)
Operating loss	(429)
Income tax	(16)
Loss after tax	(445)

The effect of the disposal of subsidiary on the financial position of the Group

	<u>2012</u>
Property and equipment (note 14)	9,055
Intangible assets (note 15)	-
Deferred tax assets (note 27)	1,731
Trade and other receivables	271
Cash and cash equivalents	172
Trade and other payables	(1)
Net assets/(liabilities)	11,228

Gain on disposal of subsidiary

	<u>2012</u>
Fair value of shares in associate	18,698
Net assets	(11,228)
Gain on disposal of subsidiary	7,470
Loss after tax	(445)
Gain on disposal of subsidiary	7,470
Net profit on disposal of subsidiary	7,025

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 33 – SUBSEQUENT EVENTS

There are no subsequent events that require financial statements adjustment or additional disclosures in financial statements.

NOTE 34 – RELATED PARTY TRANSACTIONS

The Group enters into transactions with the associated company Zdravstvena ustanova Ljekarne Jagatić and related parties Pliva Hrvatska d.o.o., Zagreb, Laguna Novigrad d.d., Novigrad, and Auctor d.o.o., Zagreb. Pliva Hrvatska d.o.o., Zagreb has a 25.32% ownership interest in the Company, however, according to operating business transactions with the Group, it has a significant impact on the Group's current business operations.

Related party transactions relating to balances in the statement of financial position as at 31 December 2012 and 2011 and transactions in the income statement for years then ended are as follows:

<i>(in thousands of HRK)</i>	<u>Note</u>	<u>2012</u>	<u>2011</u>
Trade receivables			
Associated company		19,907	13,835
Pliva Hrvatska d.o.o.. Zagreb		223	45
	18	<u>20,130</u>	<u>13,880</u>
Inventories			
Pliva Hrvatska d.o.o.. Zagreb	19	15,253	27,125
Trade payables			
Associated company		135	-
Pliva Hrvatska d.o.o.. Zagreb		165,181	129,013
	25	<u>165,316</u>	<u>129,013</u>
Sales and other revenue			
Associated company		27,771	25,248
Pliva Hrvatska d.o.o., Zagreb		267	-
	6	<u>28,038</u>	<u>25,248</u>
Gain on disposal of subsidiary and incorporation of the associate	16	7,470	-
Purchases			
Pliva Hrvatska d.o.o.. Zagreb		177,080	166,938
Key management compensation - salaries and bonuses for five members		7,429	7,337
Supervisory Board compensation		747	734

MEDIKA d.d.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2012

NOTE 34 – RELATED PARTY TRANSACTIONS (continued)

Incorporation of the associate Litums d.o.o.: The remainder of 58.47% of shares in the newly formed company is owned by Laguna Novigrad d.d. Laguna Novigrad d.d. is a related party through the company Auctor d.o.o. The effect of incorporation the associate on financial position and the operations of the Company is shown in note 16.

During the year the Company received and repaid loans in the amount of HRK 16 million from other related parties. Interest expense on loans receivable amounted to HRK 181 thousand.

Increase of share in associate ZU Ljekarne Jagatić: An increase of share was performed by introducing a pharmaceutical licence, i.e. transferring the licence and corresponding pharmaceutical unit from ZU Ljekarne Prima Pharme to associate ZU Ljekarne Jagatić (note 16).
