

**DALEKOVOD d.d.**

**AUDITOR'S REPORT AND  
FINANCIAL STATEMENTS  
31 DECEMBER 2007**

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

**Independent auditor's report**

**To the shareholders of DALEKOVOD d.d.**

We have audited the accompanying financial statements of DALEKOVOD d.d. and its subsidiaries (the 'Group') and of DALEKOVOD d.d. (the 'Company') which comprise the balance sheet as of 31 December 2007 and the income statement, statement of changes in equity and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory notes.

***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

***Auditor's Responsibility***

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

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

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

***Opinion***

In our opinion, the accompanying consolidated and non-consolidated financial statements present fairly, in all material respects, the financial position of the Group and the Company as of 31 December 2007, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.



PricewaterhouseCoopers d.o.o.  
Zagreb, 9 May 2008

**DALEKOVOD d.d.****INCOME STATEMENT****FOR THE YEAR ENDED 31 DECEMBER 2007**

<i>(all amounts are expressed in thousands of HRK)</i>	<b>Note</b>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
		<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Sales	5	1,848,513	1,534,163	1,739,227	1,513,013
Other income	6	15,423	7,229	27,351	21,555
		<b>1,863,936</b>	<b>1,541,392</b>	<b>1,766,578</b>	<b>1,534,568</b>
Change in work in progress and finished goods		15,560	(36,528)	17,102	(38,221)
Cost of goods sold		(133,441)	(81,440)	(127,918)	(73,764)
Cost of materials and services	7	(1,072,808)	(843,022)	(1,055,843)	(885,747)
Staff costs	8	(361,585)	(305,192)	(308,049)	(267,890)
Depreciation and amortisation	15,16,17	(42,082)	(35,833)	(37,197)	(32,586)
Other operating expenses	9	(144,011)	(124,049)	(132,337)	(118,075)
Other (losses)/gains – net	10	(2,812)	(2,909)	(2,938)	(2,621)
<b>Operating profit</b>		<b>122,757</b>	<b>112,419</b>	<b>119,398</b>	<b>115,664</b>
Finance income	11	4,282	1,022	3,640	685
Finance costs	11	(25,228)	(19,120)	(22,276)	(18,607)
		(20,946)	(18,098)	(18,636)	(17,922)
Profit before tax		<b>101,811</b>	<b>94,321</b>	<b>100,762</b>	<b>97,742</b>
Income tax expense	12	(21,920)	(23,083)	(21,564)	(22,875)
<b>Net profit</b>		<b>79,891</b>	<b>71,238</b>	<b>79,198</b>	<b>74,867</b>
<b>Attributable to:</b>					
Equity holders of the Company		80,360	72,324	79,198	74,867
Minority interest		(469)	(1,086)	-	-
<b>Net profit</b>		<b>79,891</b>	<b>71,238</b>	<b>79,198</b>	<b>74,867</b>
<b>Earnings per share – basic and diluted (in HRK)</b>	13	<b>35.42</b>	<b>31.88</b>	<b>34.91</b>	<b>32.96</b>

The financial statements set out on pages 2 to 52 were approved by the Management Board on 21 April 2008.

President of the Board/General Manager:

Luka Miličić M. Sc. C. E

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

**DALEKOVOD d.d.****BALANCE SHEET****AS AT 31 DECEMBER 2007**

<i>(all amounts are expressed in thousands of HRK)</i>	<b>Note</b>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
		<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
<b>ASSETS</b>					
<b>Non-current assets</b>					
Intangible assets	15	22,725	9,697	19,379	9,697
Property, plant and equipment	16	498,507	411,633	281,505	250,940
Prepayments for property, plant and equipment	16	129	1,273	46	1,273
Investment property	17	-	-	122,003	98,341
Investments in subsidiaries	18	273	253	60,643	31,076
Available-for-sale financial assets	19	27,435	7,485	27,435	7,485
Loans and receivables	21	21,762	14,767	21,373	14,767
		<u>570,831</u>	<u>445,108</u>	<u>532,384</u>	<u>413,579</u>
<b>Current assets</b>					
Inventories	22	266,566	195,004	229,023	161,130
Trade and other receivables	23	820,309	557,023	837,264	617,412
Financial assets at fair value through profit or loss	24	916	6,687	894	6,687
Cash and cash equivalents	25	186,211	29,425	177,495	17,397
		<u>1,274,002</u>	<u>788,139</u>	<u>1,244,676</u>	<u>802,626</u>
<b>Total assets</b>		<b><u>1,844,833</u></b>	<b><u>1,233,247</u></b>	<b><u>1,777,060</u></b>	<b><u>1,216,205</u></b>
<b>SHAREHOLDERS' EQUITY AND LIABILITIES</b>					
<b>Shareholders' equity</b>					
Share capital	26	229,381	229,381	229,381	229,381
Legal reserves		12,236	11,487	11,487	11,487
Treasury shares		(1,244)	(1,244)	(1,244)	(1,244)
Statutory reserves		173,309	127,459	173,309	127,459
Revaluation reserves		5,064	-	5,064	-
Other reserves		33,332	31,773	32,292	32,291
Retained earnings		80,360	73,057	79,198	74,867
		<u>532,438</u>	<u>471,913</u>	<u>529,487</u>	<u>474,241</u>
<b>Minority interest</b>		19,304	13,754	-	-
<b>Total equity</b>		<b><u>551,742</u></b>	<b><u>485,667</u></b>	<b><u>529,487</u></b>	<b><u>474,241</u></b>
<b>Non-current liabilities</b>					
Borrowings	27	195,227	182,899	174,174	173,242
Provisions	29	6,540	7,273	6,540	7,273
		<u>201,767</u>	<u>190,172</u>	<u>180,714</u>	<u>180,515</u>
<b>Current liabilities</b>					
Borrowings	27	339,972	219,324	327,073	218,344
Trade and other payables	28	750,045	332,615	738,751	337,647
Income tax payable		1,307	5,469	1,035	5,458
		<u>1,091,324</u>	<u>557,408</u>	<u>1,066,859</u>	<u>561,449</u>
<b>Total liabilities</b>		<b><u>1,293,091</u></b>	<b><u>747,580</u></b>	<b><u>1,247,573</u></b>	<b><u>741,964</u></b>
<b>Total shareholders' equity and liabilities</b>		<b><u>1,844,833</u></b>	<b><u>1,233,247</u></b>	<b><u>1,777,060</u></b>	<b><u>1,216,205</u></b>

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

**DALEKOVOD d.d.**

**STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY**

**FOR THE YEAR ENDED 31 DECEMBER 2007**

**Dalekovod Group**

*(all amounts are expressed in thousands of HRK)*

	<b>Note</b>	<b>Share capital</b>	<b>Legal reserves</b>	<b>Treasury shares</b>	<b>Statutory reserves</b>	<b>Revaluation reserves</b>	<b>Other reserves</b>	<b>Retained earnings</b>	<b>Minority interest</b>	<b>Total</b>
<b>Year ended 31 December 2006</b>										
At 1 January 2006		229,381	11,487	(1,244)	84,085	-	33,885	71,879	14,605	444,078
Currency translation differences		-	-	-	-	-	(867)	-	235	(632)
Net income recognised directly in equity		-	-	-	-	-	(867)	-	235	(632)
Net profit for the year		-	-	-	-	-	-	72,324	(1,086)	71,238
Total income recognised for 2006		-	-	-	-	-	(867)	72,324	(851)	70,606
Transfer to statutory reserves	26	-	-	-	43,374	-	-	(43,374)	-	-
Dividend relating to 2005	14	-	-	-	-	-	-	(29,017)	-	(29,017)
Transfer from other reserves		-	-	-	-	-	(1,245)	1,245	-	-
<b>At 31 December 2006</b>		<b>229,381</b>	<b>11,487</b>	<b>(1,244)</b>	<b>127,459</b>	<b>-</b>	<b>31,773</b>	<b>73,057</b>	<b>13,754</b>	<b>485,667</b>
<b>Year ended 31 December 2007</b>										
At 1 January 2007		229,381	11,487	(1,244)	127,459	-	31,773	73,057	13,754	485,667
Currency translation differences		-	-	-	-	-	4,118	-	(303)	3,815
Net costs recognised directly in equity		-	-	-	-	-	4,118	-	(303)	3,815
Net profit for the year		-	-	-	-	-	-	80,360	(469)	79,891
Total income recognised for 2007		-	-	-	-	-	4,118	80,360	(772)	83,706
Financial assets – fair value	26	-	-	-	-	5,064	-	-	-	5,064
Capital contribution to Unidal d.o.o.	18	-	-	-	-	-	-	-	3,474	3,474
Minority interests – acquisition of TIM d.d.	30	-	-	-	-	-	-	-	2,848	2,848
Transfer to reserves	26	-	749	-	45,850	-	-	(46,599)	-	-
Dividend relating to 2006	14	-	-	-	-	-	-	(29,017)	-	(29,017)
Transfer from other reserves		-	-	-	-	-	(2,559)	2,559	-	-
<b>At 31 December 2007</b>		<b>229,381</b>	<b>12,236</b>	<b>(1,244)</b>	<b>173,309</b>	<b>5,064</b>	<b>33,332</b>	<b>80,360</b>	<b>19,304</b>	<b>551,742</b>

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

**DALEKOVOD d.d.****STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY****FOR THE YEAR ENDED 31 DECEMBER 2007****Dalekovod d.d.***(all amounts are expressed in thousands of HRK)*

	<b>Note</b>	<b>Share capital</b>	<b>Legal reserves</b>	<b>Treasury shares</b>	<b>Revaluation reserves</b>	<b>Statutory reserves</b>	<b>Other reserves</b>	<b>Retained earnings</b>	<b>Total</b>
<b>Year ended 31 December 2006</b>									
At 1 January 2006		229,381	11,487	(1,244)	-	84,085	32,291	72,391	428,391
Dividend relating to 2005	14	-	-	-	-	-	-	(29,017)	(29,017)
Statutory reserves		-	-	-	-	43,374	-	(43,374)	-
Net profit		-	-	-	-	-	-	74,867	74,867
<b>At 31 December 2006</b>	<b>25</b>	<b>229,381</b>	<b>11,487</b>	<b>(1,244)</b>	<b>-</b>	<b>127,459</b>	<b>32,291</b>	<b>74,867</b>	<b>474,241</b>
<b>Year ended 31 December 2007</b>									
At 1 January 2007		229,381	11,487	(1,244)	-	127,459	32,291	74,867	474,241
Dividend relating to 2006		-	-	-	-	-	-	(29,016)	(29,016)
Financial assets – fair value		-	-	-	5,064	-	-	-	5,064
Statutory reserves		-	-	-	-	45,850	1	(45,851)	-
Net profit		-	-	-	-	-	-	79,198	79,198
<b>At 31 December 2007</b>		<b>229,381</b>	<b>11,487</b>	<b>(1,244)</b>	<b>5,064</b>	<b>173,309</b>	<b>32,292</b>	<b>79,198</b>	<b>529,487</b>

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

**DALEKOVOD d.d.**

**CASH FLOW STATEMENT**

**FOR THE YEAR ENDED 31 DECEMBER 2007**

<i>(all amounts are expressed in thousands of HRK)</i>	Note	Dalekovod Group		Dalekovod d.d.	
		2007	2006	2007	2006
<b>Cash flows from operating activities</b>					
Cash generated from operations	31	341,669	24,093	336,087	18,368
Interest paid		(28,689)	(18,233)	(21,886)	(17,774)
Income tax paid		(27,389)	(23,974)	(25,988)	(23,777)
<b>Net cash inflow (outflow) from operating activities</b>		<b>285,591</b>	<b>(18,114)</b>	<b>288,213</b>	<b>(23,183)</b>
<b>Cash flows from investing activities</b>					
Purchase of intangible assets	15	(10,823)	(4,707)	(10,823)	(4,707)
Purchase of property, plant and equipment		(108,966)	(97,498)	(93,406)	(81,183)
Proceeds from sale of property, plant and equipment	31	3,123	853	2,699	852
Loans granted		(74,724)	(17,459)	(74,134)	(21,336)
Loan repayments received		11,818	17,746	12,209	17,468
Investment in subsidiaries and associate		(30)	(28)	(29,577)	(2,848)
Investment in available-for-sale financial assets	19	(14,876)	(739)	(14,876)	(739)
Acquisition of subsidiary	30	(23,777)	-	-	-
Sale of/investment in financial assets		5,894	(6,350)	5,916	(6,350)
Interest received		6,034	3,037	6,180	3,081
<b>Net cash used in investing activities</b>		<b>(206,327)</b>	<b>(105,145)</b>	<b>(195,812)</b>	<b>(95,762)</b>
<b>Cash flows from financing activities</b>					
Proceeds from borrowings		414,433	252,550	384,380	237,942
Issue of commercial papers	27	32,000	75,000	32,000	75,000
Repayments of borrowings		(325,519)	(212,993)	(305,291)	(208,661)
Dividends paid		(43,392)	(14,878)	(43,392)	(14,878)
<b>Net cash from financing activities</b>		<b>77,522</b>	<b>99,679</b>	<b>67,697</b>	<b>89,403</b>
<b>Net increase/(decrease) in cash and cash equivalents</b>		<b>156,786</b>	<b>(23,580)</b>	<b>160,098</b>	<b>(29,542)</b>
Cash and cash equivalents at beginning of year		29,425	53,005	17,397	46,939
Cash and cash equivalents at end of year	25	186,211	29,425	177,495	17,397
<b>Net increase/(decrease) in cash and cash equivalents</b>		<b>156,786</b>	<b>(23,580)</b>	<b>160,098</b>	<b>(29,542)</b>

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

**NOTE 1 – GENERAL INFORMATION**

The Dalekovod Group (the Group) comprises the parent company Dalekovod d.d., Zagreb and eight subsidiaries (2006: seven) – Note 18.

Dalekovod d.d., Zagreb (the Company) is privately owned and was incorporated in compliance with the laws and regulations of the Republic of Croatia. The registered office of the Company is in Zagreb, Marijana Čavića 4. As at 31 December 2007, the Company's shares were listed on the public joint stock company listing on the Zagreb Stock Exchange.

The Company's principal activity is the engineering, production, construction and installation of electric power facilities, facilities for road, railroad and mass transit and telecommunication infrastructure.

**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. All policies applicable to the Group are also applicable to the Company, unless otherwise stated.

**2.1 Basis of preparation**

The financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS) under the historical cost convention, as modified by financial assets at fair value through profit or loss and available for sale financial assets.

The preparation of 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 where assumptions and estimates are significant to the consolidated financial statements, are disclosed in Note 4.

*(a) Standards and interpretations early adopted by the Company and the Group*

No standards were early adopted by the Group and the Company.

*(b) Standards and interpretations to existing standards effective in 2007 and relevant to the Company's and the Group's operations*

- *IFRS 7, Financial instruments: Disclosures, and the complementary amendment to IAS 1, Presentation of financial statements – Capital disclosures*, introduces new disclosures relating to financial instruments (Notes: 3, 20.a and 20.b) and does not have any impact on the classification and valuation of the Group's and the Company's financial instruments.

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.1 Basis of preparation (continued)**

*(c) Standards, amendments and interpretations effective in 2007 but not relevant for the Company and the Group*

The following standards, amendments and interpretations to existing standards are mandatory for accounting periods beginning on or after 1 January 2007, but they are not relevant to the Company's and the Group's operations:

- *IFRIC 7, Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies.* IFRIC 7 is not relevant as the Company and the Group do not operate in a hyperinflationary environment.
- *IFRIC 8, Scope of IFRS 2.* IFRIC 8 is not relevant since the Company and the Group do not have share-based payments.
- *IFRIC 9, Reassessment of embedded derivatives.* IFRIC 9 is not relevant to the Company's and the Group's operations because they do not have any embedded derivatives.
- *IFRIC 10, Interim Financial Reporting and Impairment.* IFRIC 10 is not relevant to the Company's and the Group's operations because interim financial reports are not produced.

*(d) Standards and interpretations to existing standards that are not yet effective and have not been early adopted by the Company and Group*

The following standards and interpretations to existing standards are mandatory for the Company's and Group's accounting period beginning on or after the effective date, but the Company and the Group have not early adopted them:

- *IFRS 8, Operating segments (effective from 1 January 2009).* The standard applies to entities whose debt or equity instruments are traded in a public market or that file, or are in the process of filing, their financial statements with a regulatory organisation for the purpose of issuing any class of instruments in a public market. IFRS 8 requires an entity to report financial and descriptive information about its operating segments and specifies how an entity should report such information. Management is currently assessing what impact the standard will have on segment disclosures in the Group's financial statements.
- *IAS 23 (revised), Borrowing costs (effective from 1 January 2009).* The revised IAS 23 was issued in March 2007. The main change to IAS 23 is the removal of the option of immediately recognising as an expense borrowing costs that relate to assets that take a substantial period of time to get ready for use or sale. An entity is, therefore, required to capitalise such borrowing costs as part of the cost of the asset. The revised standard applies prospectively to borrowing costs relating to qualifying assets for which the commencement date for capitalisation is on or after 1 January 2009. The Group is currently assessing the impact of the amended standard on its financial statements.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

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NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2.1 Basis of preparation (continued)

(d) *Standards and interpretations to existing standards that are not yet effective and have not been early adopted by the Company and Group – continued*

- *IAS 27, Consolidated and Separate Financial Statements (revised January 2008; effective for annual periods beginning on or after 1 July 2009)*. The revised IAS 27 will require an entity to attribute total comprehensive income to the owners of the parent and to the non-controlling interests (previously minority interests) even if this results in the non-controlling interests having a deficit balance. The current standard requires excess losses to be allocated to the owners of the parent, except to the extent that the non-controlling interests have a binding obligation and are able to make an additional investment to cover the losses. The revised standard also specifies that changes in a parent's ownership interest in a subsidiary that do not result in the loss of control must be accounted for as equity transactions. It also specifies how an entity should measure any gain or loss arising on the loss of control of a subsidiary. Any investment retained in the former subsidiary will have to be measured at its fair value at the date when control is lost. The current standard requires the carrying amount of an investment retained in the former subsidiary to be regarded as its cost on initial measurement of the financial asset in accordance with IAS 39, *Financial Instruments: Recognition and Measurement*. The Group is currently assessing the impact of the amended standard on its financial statements.
- *IFRS 3 (revised), Business Combinations (effective from or after 1 July 2009)*. The Group is currently assessing the impact of the amended standard on its financial statements.

(e) *Interpretations to existing standards that are not yet effective and are not relevant to the Company's and Group's operations*

The following interpretations to existing standards are mandatory for the *Company's and Group's* accounting period beginning on or after 1 January 2008, but are not currently relevant to the *Company's and Group's* operations:

- *Vesting Conditions and Cancellations – Amendment to IFRS 2, Share-based Payment (issued in January 2008; effective for annual periods beginning on or after 1 January 2008)*. This amendment is not relevant since the Group does not have share-based payments.
- *IFRIC 12, Service Concession Arrangements (effective annual periods beginning on or after 1 January 2008)*. IFRIC 12 is not relevant since the Group is not an operator of a public-to-private service concession arrangement.
- *IFRIC 13, Customer loyalty programmes (effective from 1 July 2008)*. IFRIC 13 is not relevant, since the Group does not operate such programmes.
- *IFRIC 14, IAS 19, The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction (effective from 1 January 2008)*. IFRIC 14 is not relevant since the Group does not have defined benefit plans.

**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 (acquisition date). They are de-consolidated from the date that control ceases.

In the non-consolidated financial statements, the Company carries investments in subsidiaries at acquisition cost.

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. The date of exchange is the acquisition date where a business combination is achieved in a single transaction, and is the date of each share purchase where a business combination is achieved in stages by successive share purchases.

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

*(b) Transactions and minority interests*

The Group applies a policy of treating transactions with minority interests as transactions with parties external to the Group. Disposals to minority interests result in gains and losses for the Group that are recorded in the income statement. Purchases from minority interests result in goodwill, being the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary.

**2.3 Segment reporting**

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

**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 Group's functional and presentation currency.

*(b) Transactions and balances*

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.

*(c) Group companies*

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

- (i) assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- (ii) income and expenses for each income statement are translated at average exchange rates; and
- (iii) all resulting exchange differences are recognised as a separate component of equity.

On consolidation, exchange differences arising from the translation of the net investment in foreign operations are taken to 'Cumulative translation reserves' within shareholders' equity. When a foreign operation is partially disposed of or sold, exchange differences that were recorded in equity are recognised in the income statement as part of the gain or loss on sale.

**2.5 Property, plant and equipment**

Property, plant and equipment is included in the balance sheet at historical cost less accumulated depreciation and provision for impairment, where required. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

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.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

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NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

**2.5 Property, plant and equipment (continued)**

Land and work in progress are not depreciated. Depreciation of other assets is calculated using the straight-line method to allocate their cost to their residual values over their estimated useful lives, as follows:

	<u>Useful lives in years</u>
Buildings	20 – 40
Plant, machinery and equipment	8 – 10
Transportation vehicles	5 – 8
Leasehold improvements	Over the term of the underlying lease
Other	5 – 10

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 were 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 balance sheet date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 2.8).

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the line item "other (losses)/gains – net" in the income statement.

**2.6 Investment properties**

Investment property, principally comprising office buildings and land, is held for long-term rental yields or appreciation and is not occupied by the Group. Investment property is treated as a long-term investment unless it is intended to be sold in the next year and a buyer has been identified in which case it is classified within current assets.

Investment property is carried at historical cost less accumulated depreciation and provision for impairment, where required. Depreciation for buildings is calculated using the straight-line method to allocate cost over estimated useful life (20 to 40 years).

Subsequent expenditure is capitalised only when it is probable that future economic benefits associated with it will flow to the Group and the cost can be measured reliably. All other repairs and maintenance costs are expensed when incurred. If an investment property becomes owner-occupied, it is reclassified to property, plant and equipment, and its carrying amount at the date of reclassification becomes its deemed cost to be subsequently depreciated.

**2.7 Intangible assets**

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 years).

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.8 Impairment of non-financial assets**

Assets that have an indefinite useful life (such as land or goodwill) are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation and depreciation 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.

**2.9 Financial assets**

The Group and the Company classify their financial assets in the following categories: at fair value through profit or loss, available-for-sale financial assets and loans and 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.

*(a) Financial assets at fair value through profit or loss*

Financial assets at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term. Assets in this category are classified as current assets.

Financial assets carried at fair value through profit or loss are initially recognised at fair value and transaction costs are expensed in the income statement.

Gains or losses arising, from changes in the fair value of the 'financial assets at fair value through profit or loss' category are presented in the income statement within the line item 'other (losses)/gains – net' in the period in which they arise.

*(b) Available-for-sale financial assets*

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories. They are included in non-current assets unless management intends to dispose of the investment within 12 months of the balance sheet date. Available-for-sale financial assets are carried at fair value.

Changes in the fair value of monetary securities and non-monetary securities classified as available-for-sale are recognised in equity.

In the case of equity securities classified as available for sale, a significant or prolonged decline in the fair value of the security below its cost is considered as an indicator that the securities are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from equity and recognised in the income statement.

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.9 Financial assets (continued)**

*(b) Available-for-sale financial assets (continued)*

When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognised in equity are included in the income statement in line item 'other (losses)/gains – net'.

Interest on available-for-sale securities calculated using the effective interest rate method is recognised in the income statement. Dividends on available-for-sale securities are recognised in the income statement when the right to receive payment is established.

The Group and the Company assess at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement.

*(c) Loans and receivables*

Loans and 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 balance sheet date. These are classified as non-current assets.

Loans and receivables are carried at amortised cost using the effective interest method. Impairment testing of loans and receivables is described in Note 2.12.

**2.10 Leases**

*The Group and the Company are the lessee*

The Group and the Company lease certain property, plant and equipment. Leases of property, plant and equipment, where the Group or the Company has substantially all the risks and rewards of ownership, are classified as finance leases. Finance leases are capitalized at the lease's commencement 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 in which a significant portion of risks and rewards of ownership are retained by the lessor 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.

*The Group and the Company are the lessor*

Assets under an operating lease are depreciated over their expected useful lives on a basis consistent with similar owned assets. Rental income is recognised on a straight-line basis over the lease term, even if the proceeds are not balanced, unless there is an alternative basis representing the time frame in which the benefits of the lease and the depreciation of the leased property are matched.

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.11 Inventories**

Inventories of raw materials and spare parts are stated at the lower of cost, determined using the weighted average method, or net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

The cost of work-in-process and finished goods comprise raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity).

Small inventory and tools are expensed when put into use.

**2.12 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 and the Company 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".

**2.13 Construction contracts**

Contract costs are recognised when incurred.

When the outcome of a construction contract cannot be estimated reliably, contract revenue is recognised only to the extent of contract costs incurred that are likely to be recoverable.

When the outcome of a construction contract can be estimated reliably and it is probable that the contract will be profitable, contract revenue is recognised over the period of the contract. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately.

The Group and the Company use the 'percentage of completion method' to determine the appropriate amount to recognise in a given period. The stage of completion is measured by reference to the contract costs incurred up to the balance sheet date as a percentage of total estimated costs for each contract. Costs incurred in the year in connection with future activity on a contract are excluded from contract costs in determining the stage of completion. They are presented as inventories, prepayments or other assets, depending on their nature.

The Group and the Company present as an asset the gross amount due from customers for contract work for all contracts in progress for which costs incurred plus recognised profits (less recognised losses) exceed progress billings. Progress billings not yet paid by customers and retention are included within 'trade and other receivables'.

The Group presents as a liability the gross amount due to customers for contract work for all contracts in progress for which progress billings exceed costs incurred plus recognised profits (less recognised losses).

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

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**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.14 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.

**2.15 Share capital**

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Where 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.

**2.16 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. The Group and the Company do not capitalise borrowing costs.

Borrowings are classified as current liabilities unless the Group and the Company have an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

**2.17 Deferred income tax**

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 income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income 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.

**2.18 Trade and other payables**

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

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.19 Employee benefits**

*(a) Pension obligations and post-employment benefits*

In the normal course of business through salary deductions, the Group and the Company make 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.

Furthermore, according to Collective bargaining agreement the Group and the Company have an obligation to make severance payments to employees at the time of the employees' retirement. The liability recognised in the balance sheet is the present value of defined benefit obligation at the balance sheet date less past service costs with adjustments for unrecognised actuarial gains or losses. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of governmental bonds that are denominated in the currency in which the benefits will be paid and that have terms to maturity approximating to the terms of the related retirement severance payment.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions in excess of 10% of the defined benefit obligation are charged or credited to income over the employee's expected average remaining working lives.

Past-service costs are amortised on a straight-line basis over the employee's expected average remaining working life.

In addition, the Group is not obliged to provide any other post-employment benefits.

*(b) Termination benefits*

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. Benefits falling due more than 12 months after the balance sheet date are discounted to present value.

*(c) Long-term employee benefits*

The Group recognises a liability for long-term employee benefits evenly over the period the benefit is earned based on actual years of service. The long-term employee benefit liability is determined using assumptions regarding the likely number of staff to whom the benefit will be payable, estimated benefit cost and the discount rate.

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.20 Provisions**

Provisions 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.

Where 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 one 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 increase in the provision due to passage of time is recognised as interest expense.

**2.21 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 and the Company's activities. Revenue is shown, net of value-added tax, estimated returns, rebates and discounts. The Group and the Company recognise 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 and the Company's activities as described below.

*(a) Revenue from construction contracts*

When the outcome of a construction contract cannot be estimated reliably, contract revenue is recognised only to the extent of contract costs incurred that are likely to be recoverable. When the outcome of a construction contract can be estimated reliably and it is probable that the contract will be profitable, contract revenue is recognised over the period of the contract (Note 2.12).

*(b) Sales of goods*

Sales of goods are recognised when the Group and the Company have delivered products to the customer, the customer has accepted the products and collectibility of the related receivables is reasonably assured.

*(c) Interest income*

Interest income is recognised on a time-proportion basis using the effective interest method. When a receivable is impaired, the Group and the Company reduce the carrying amount to its recoverable amount, being the estimated future cash flow discounted at original effective interest rate of the instrument, and continues unwinding the discount as interest income. Interest income on impaired loans is recognised using the original effective interest rate.

*(d) Dividend income*

Dividend income is recognised when the right to receive payment is established.

**NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.22 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 General Meeting of the Company's shareholders.

**2.23 Earnings per share**

Earnings per share is determined by dividing the profit or loss attributable to equity holders of the Company by the weighted average number of participating shares outstanding during the reporting year.

**2.24 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 balance sheet on a net basis. Where provision has been made for impairment of receivables, impairment loss is recorded for the gross amount of the debtor, including VAT.

**2.25 Comparatives**

Where necessary, corresponding figures have been adjusted to conform with changes in the presentation of the current year. Management believes that this is a better presentation and in compliance with disclosed accounting policies. Foreign revenues in 2006 were shown net of costs of goods sold arising from the re-export of goods to foreign countries. The total effect of this presentation was a decrease in foreign sales revenue by HRK 81,440 thousand for the Group and HRK 73,764 thousand for the Company.

**NOTE 3 – FINANCIAL RISK MANAGEMENT**

**3.1 Financial risk factors**

The Company's and the Group's activities expose them to a variety of financial risks: market risk (including currency risk and cash flow interest rate risk), credit risk and liquidity risk. The Group and the Company do not have a written risk management programme, but overall risk management in respect of these risks is carried out by the Company's finance department.

(a) Market risk

(i) *Foreign exchange risk*

The majority of foreign sales revenue is denominated in EUROS and USD. Domestic sales revenue is denominated in HRK. The majority of long-term and short-term loans were agreed with a currency clause, i.e. they are linked to the EURO. Any movement in exchange rates between the EURO and USD against the Croatian kuna will have an impact on the Group's and the Company's operating results.

At 31 December 2007, if the EURO had weakened/strengthened by 0.5% against the HRK, with all other variables held constant, the net profit for the reporting period after tax would have been HRK 6,905 thousand (2006: HRK 3,499 thousand) higher/(lower), mainly as a result of foreign exchange gains/(losses) on translation of EURO-denominated trade receivables, borrowings and foreign cash funds.

At 31 December 2007, if the USD had weakened/strengthened by 5% against the HRK, with all other variables held constant, the net profit for the reporting period after tax would have been HRK 8,097 thousand (2006: HRK 510 thousand) higher/(lower), mainly as a result of foreign exchange gains/(losses) on translation of USD-denominated trade receivables, prepayments and foreign cash funds.

(ii) *Equity securities risk*

The Group is exposed to equity securities fair value and price risk because of investments held by the Group classified on the consolidated balance sheet either as available for sale or at fair value through profit or loss. Equity investments classified as available for sale are not listed, while those classified as fair value through profit or loss are publicly traded. To manage its fair value and price risk arising from investments in equity securities, the Group monitors market transactions and performance of investment entities.

**NOTE 3 – FINANCIAL RISK MANAGEMENT (continued)**

**3.1 Financial risk factors (continued)**

*(iii) 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 and the Company's interest rate risk arises from long-term borrowings and commercial papers. Borrowings issued at variable rates expose the Group and the Company to cash flow interest rate risk. Borrowings issued at fixed rates expose the Group to fair value interest rate risk (Note 27).

The Group and the Company analyse their interest rate changes on a regular basis. Various scenarios are simulated taking into consideration refinancing, renewal of existing positions and alternative financing. Based on these scenarios, the Group and the Company calculate the impact on profit and loss of a defined interest rate shift. As at 31 December 2007, if the effective interest rate on borrowings had increased/decreased by 1% on an annual level (2006: 1%), the profit after tax would be lower/higher by HRK 4,938 thousand (2006: HRK 4,214 thousand).

*(b) Credit risk*

The Group's assets, which potentially subject the Group to concentrations of credit risk, primarily include cash, trade and other receivables. The Group has policies in place to ensure that sales of products are made to customers with an appropriate credit history, within previously defined credit limits. A favourable structure of buyers and the fact that, if necessary, collection from buyers is regulated by bank payment guarantees, bills of exchange, letters of credit and other types of security, almost completely diminishes the risk arising from the collection of trade receivables. A detailed analysis and maximum exposure to credit risk are shown in Note 23.

The Group has policies that limit the amount of credit exposure to any financial institution.

*(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.

Trade and other payables as well as short-term borrowings are due within 12 months after the balance sheet date, while the maturity of long-term borrowings is disclosed in Note 27.

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 3 – FINANCIAL RISK MANAGEMENT (continued)

## 3.1 Financial risk factors (continued)

*(c) Liquidity risk (continued)*

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>	<b>Less than 1 year</b>	<b>Between 1-5 years</b>	<b>Over 5 years</b>	<b>Total</b>
<b>31 December 2007</b>				
Trade payables	443,941	-	-	443,941
Other payables	21,436	-	-	21,436
Borrowings	388,482	107,074	39,643	535,199
 <i>(in thousands of HRK)</i>				
<b>31 December 2006</b>				
Trade payables	232,158	-	-	232,158
Other payables	20,710	-	-	20,710
Borrowings	245,246	102,770	54,207	402,223

Financial liabilities do not include amounts due to employees, liabilities for contributions, taxes and advances received.

## 3.2 Capital risk management

The Company and the Group monitor capital on the basis of laws and regulations of the countries in which they operate. Croatian laws and regulations require minimum paid in capital of HRK 200 thousand for joint stock companies. There are no specific objectives required by the owners in managing capital. The Company and the Group are not subject to externally imposed capital requirements. In addition, there are no internally monitored capital objectives.

## 3.3 Fair value estimation

The fair value of financial instruments traded in active markets is based on quoted market prices at the balance sheet 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 balance sheet date.

The nominal 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 Company for similar financial instruments.

**NOTE 4 – CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS**

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, rarely 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 outlined below.

*(a) Revenue recognition*

The Group uses the percentage-of-completion method in accounting for its revenue from construction contracts to determine the appropriate amount to recognise in a given period. The stage of completion is measured by reference to the contract costs incurred up to the balance sheet date as a percentage of total estimated costs for each contract. If the estimated stage of completion would differ by 10% from management's estimates, the amount of revenue recognized in the year would be increased by HRK 5,780 thousand if the percentage of completion were increased, or would be decreased by HRK 4,971 thousand if the percentage of completion were decreased.

*(b) Long-term employee benefits*

The Group recognises non-current liabilities to employees including liabilities for jubilee awards and retirement benefits in the amount of the estimated present value of future expenses. Each year a certified actuary reevaluates the present value of these liabilities based on new information.

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 5 – SEGMENT INFORMATION

**Primary reporting format – business segments**

The Group separately monitors and presents business results of basic business segments, Production and Construction, whose operating activities are interrelated for the purpose of realising profit for the Group.

1. The segment of Production includes the forging works, the casting plant and the laboratory for quality control and the production of metal frames/structures.
2. The segment of Construction includes the construction of power and distribution facilities, transformer stations, laying submarine, subterranean and telecommunication cables, posting public lighting, installing antenna, television and telecommunication posts as well as work relating to the construction of motorways.
3. Other business segments includes separately Project design, Zinc coating facility and other activities (subsidiary activities, restaurant and common services).

*Operating results by business segments**(in thousands of HRK)*

	<u>Construction</u>	<u>Production</u>	<u>Other</u>	<u>Total</u>
<b>Year ended 31 December 2007</b>				
Gross segment revenues	1,307,577	244,472	471,327	2,023,376
Inter-segment sales	(10,660)	(36,448)	(112,332)	(159,440)
Operating revenues	1,296,917	208,024	358,995	1,863,936
Operating profit	101,797	765	20,195	122,757
Finance cost				(20,946)
Profit before tax				101,811
Income tax expense				(21,920)
<b>Net profit</b>				<b>79,891</b>
<b>Year ended 31 December 2006</b>				
Gross segment revenues	1,077,816	466,737	224,933	1,769,486
Inter-segment sales	(12,105)	(126,633)	(89,356)	(228,094)
Operating revenues	1,065,711	340,104	135,577	1,541,392
Operating profit	85,885	1,112	25,422	112,419
Finance cost				(18,098)
Profit before tax				94,321
Income tax expense				(23,083)
<b>Net profit</b>				<b>71,238</b>

## NOTES TO THE FINANCIAL STATEMENTS

## FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 5 – SEGMENT INFORMATION (continued)

Other segment information included in the income statement:

<i>(in thousands of HRK)</i>	<u>Construction</u>	<u>Production</u>	<u>Other</u>	<u>Total</u>
<b>Year ended 31 December 2007</b>				
Depreciation and amortisation (Notes 15,16)	12,112	11,305	18,665	42,082
Provision for inventories (Note 9)	160	-	87	247
Change in provision for receivables (Note 9)	588	-	212	800
Property, plant and equipment written off (Note 9)	141	2,023	309	2,473
<b>Year ended 31 December 2006</b>				
Depreciation and amortisation (Notes 15,16)	8,868	11,330	15,635	35,833
Provision for inventories (Note 9)	551	-	-	551
Change in provision for receivables (Note 9)	75	-	56	131
Property, plant and equipment written off (Note 9)	165	23	32	220

Balance sheet by business segments:

<i>(in thousands of HRK)</i>	<u>Constructio n</u>	<u>Production</u>	<u>Other</u>	<u>Unallocated</u>	<u>Total</u>
<b>At 31 December 2007</b>					
<b>Assets</b>					
Property, plant and equipment	72,869	66,894	358,744	-	498,507
Other assets	780,335	401,126	164,865	-	1,346,326
	<b>853,204</b>	<b>468,020</b>	<b>523,609</b>	<b>-</b>	<b>1,844,833</b>
<b>Liabilities</b>					
Long-term borrowings	-	-	-	195,227	195,227
Long-term provisions	-	-	-	6,540	6,540
Current liabilities	320,497	90,748	86,455	593,624	1,091,324
	<b>320,497</b>	<b>90,748</b>	<b>86,455</b>	<b>795,391</b>	<b>1,293,091</b>
<b>Capital expenditure (Notes 15 and 16)</b>	59,306	44,845	12,517	-	116,668
<b>At 31 December 2006</b>					
<b>Assets</b>					
Property, plant and equipment	66,495	126,371	218,767	-	411,633
Other assets	490,991	273,945	56,678	-	821,614
	<b>557,486</b>	<b>400,316</b>	<b>275,445</b>	<b>-</b>	<b>1,233,247</b>
<b>Liabilities</b>					
Long-term borrowings	-	-	-	182,899	182,899
Long-term provisions	-	-	-	7,273	7,273
Current liabilities	202,591	76,282	7,910	270,625	557,408
	<b>202,591</b>	<b>76,282</b>	<b>7,910</b>	<b>460,797</b>	<b>747,580</b>
<b>Capital expenditure (Notes 15 and 16)</b>	37,824	26,303	37,713	-	101,840

Non-current assets comprises land, buildings, equipment and intangible assets, whereas current assets of segments primarily comprises inventories, trade receivables and cash. Long-term loans of segments are not allocated. Current liabilities of segments primarily comprise trade payables and other operating liabilities.

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 5 – SEGMENT INFORMATION (continued)

## Secondary reporting format – geographical segments

Sales among geographical segments are allocated based on the country in which the customer is located.

	2007		2006	
	<i>(in thousands of HRK)</i>	%	<i>(in thousands of HRK)</i>	%
Croatia	1,451,247	78.51	1,281,739	83.55
Bosnia and Herzegovina	139,146	7.53	153,400	9.99
Norway	31,576	1.71	-	-
Kazakhstan	72,330	3.91	-	-
Other	154,214	8.34	99,024	6.46
<b>Total</b>	<b>1,848,513</b>	<b>100.00</b>	<b>1,534,163</b>	<b>100.00</b>

## NOTE 6 – OTHER INCOME

<i>(in thousands of HRK)</i>	Dalekovod Group		Dalekovod d.d.	
	2007	2006	2007	2006
Interest income	5,561	3,255	4,545	3,307
Proceeds from insurance claims	867	255	867	255
Rental income	8	9	15,548	14,691
Income from reversal of provisions (Note 27)	733	-	733	-
Other operating income	8,254	3,710	5,658	3,302
	<b>15,423</b>	<b>7,229</b>	<b>27,351</b>	<b>21,555</b>

Rental income mainly relates to the lease of property to the subsidiary Dalekovod-Cinčaonica d.o.o. which reimburses the depreciation charge of leased assets, the interest expense of long-term borrowings used to finance the construction of leased assets and the expense of common departments (accounting, legal affairs, etc.) providing services to the subsidiary.

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 7 – COST OF MATERIALS AND SERVICES

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<u>2007</u>	<u>2006</u>	<u>2007</u>	<u>2006</u>
<b>Raw materials and supplies</b>				
Raw materials and supplies	361,053	291,509	299,791	308,168
Energy	16,613	17,769	13,008	11,616
Spare parts and small inventory	8,455	7,525	8,536	10,780
	<u>386,121</u>	<u>316,803</u>	<u>321,335</u>	<u>330,564</u>
<b>External services</b>				
Subcontractor services	628,374	457,092	683,071	505,335
Transportation	23,891	24,592	23,086	24,087
Repairs and maintenance	10,032	10,596	8,321	10,376
Advertising and promotion	12,858	6,481	12,842	5,334
Rental expense	1,130	2,922	1,109	1,958
Other	10,402	24,536	6,079	8,093
	<u>686,687</u>	<u>526,219</u>	<u>734,508</u>	<u>555,183</u>
<b>Total cost of materials and services</b>	<b><u>1,072,808</u></b>	<b><u>843,022</u></b>	<b><u>1,055,843</u></b>	<b><u>885,747</u></b>

Rental expenses relate to the lease of vehicles and office premises based on one-year agreements.

## NOTE 8 – STAFF COSTS

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<u>2007</u>	<u>2006</u>	<u>2007</u>	<u>2006</u>
Net salaries	195,486	163,691	161,470	138,461
Taxes and contributions on and from salaries	152,206	124,632	134,014	114,233
Severance costs	5,077	4,308	5,077	4,308
Other staff costs	8,374	12,304	7,119	10,631
Supervisory Board fees	442	257	369	257
	<u>361,585</u>	<u>305,192</u>	<u>308,049</u>	<u>267,890</u>

Taxes and contributions include contributions paid into mandatory pension funds in the amount of HRK 55,581 thousand (2006: HRK 47,577 thousand) for the Group, and HRK 49,644 thousand for the Company (2006: HRK 43,334 thousand). Contributions are calculated as a percentage of the employees' gross salaries.

Other staff costs include gifts, jubilee awards and other benefits.

As at 31 December 2007, the Group had 2,190 employees (2006: 2,038 employees), and the Company had 1,558 employees (2006: 1,566).

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 9 – OTHER OPERATING EXPENSES

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Intellectual services	57,101	36,240	54,982	34,286
Daily allowances and travel cost	29,944	32,200	27,255	30,325
Bank charges	8,579	10,973	8,436	10,892
Entertainment	9,376	9,208	9,219	9,854
Taxes and contributions	7,193	8,266	7,015	7,810
Insurance	6,569	5,024	6,288	4,897
Sponsorships, donations and other aids	8,652	5,289	8,610	5,462
Write-off of property, plant and equipment	2,473	220	2,175	221
Change in provision for impairment of trade receivables	800	131	588	(499)
Write-off of inventories	247	551	160	551
Write-off of loan receivables	-	2,441	-	2,441
Other operating expenses	13,077	13,506	7,609	11,835
	<b>144,011</b>	<b>124,049</b>	<b>132,337</b>	<b>118,075</b>

## NOTE 10 – OTHER (LOSSES)/GAINS – NET

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Net foreign exchange (loss)/gain from operating activities	(3,585)	(3,240)	(3,585)	(3,197)
Fair value gains (Note 24)	123	337	123	337
Net (loss)/gain on sale of tangible assets (Note 31)	650	(6)	524	239
	<b>(2,812)</b>	<b>(2,909)</b>	<b>(2,938)</b>	<b>(2,621)</b>

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 11 – FINANCE INCOME AND COSTS

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Interest income on bank deposits	1,162	170	1,162	170
Net foreign exchange differences (financing activities)	3,120	852	2,478	515
Finance income	<u>4,282</u>	<u>1,022</u>	<u>3,640</u>	<u>685</u>
Net foreign exchange difference on bank deposits	-	(36)	-	(36)
Interest expense	<u>(25,228)</u>	<u>(19,084)</u>	<u>(22,276)</u>	<u>(18,571)</u>
Finance cost	<u>(25,228)</u>	<u>(19,120)</u>	<u>(22,276)</u>	<u>(18,607)</u>
	<b><u>(20,946)</u></b>	<b><u>(18,098)</u></b>	<b><u>(18,636)</u></b>	<b><u>(17,922)</u></b>

## NOTE 12 – INCOME TAX

The reconciliation of accounting income and taxable income is detailed in the table below:

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
<b>Net profit before tax</b>	<b><u>101,811</u></b>	<b><u>94,321</u></b>	<b><u>100,763</u></b>	<b><u>97,742</u></b>
Tax calculated at a rate of 20%	20,362	18,864	20,153	19,548
Effect of income not subject to tax	(503)	(444)	(341)	(444)
Effect of expenses not deductible for tax purposes	1,834	4,456	1,752	3,771
Effect of tax rates in other countries	<u>272</u>	<u>207</u>	<u>-</u>	<u>-</u>
<b>Income tax charge</b>	<b><u>21,920</u></b>	<b><u>23,083</u></b>	<b><u>21,564</u></b>	<b><u>22,875</u></b>
Effective tax rate	21.53%	24.47%	21.40%	23.4%
Income tax payable as at 31 December	1,307	5,469	1,035	5,458

During 2006, the Tax Authority performed an audit of the Company's income tax charged for 2005 and did not establish any additional tax liability. In accordance with the regulations of the Republic of Croatia, the Tax Authority may at any time inspect the Company's books and records within 3 years following the year in which the tax liability is reported, and may impose additional tax assessments and penalties. The same regulations apply to other subsidiaries of the Group in Croatia. Foreign subsidiaries abroad must comply with tax regulations of the country in which they operate. The Group's management is not aware of any circumstances, which may give rise to a potential material liability in this respect.

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

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**NOTE 13 – BASIC AND DILUTED EARNINGS PER SHARE**

Basic earnings per share are calculated on the basis of the Group's and the Company's net profit and the weighted average number of ordinary shares in issue, excluding treasury shares. There are no dilutable potential ordinary shares.

	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Net profit ( <i>in thousands of HRK</i> )	80,360	72,324	79,198	74,867
Weighted average number of shares	2,268,573	2,268,984	2,268,573	2,268,984
<b>Earnings per share (<i>in HRK</i>)</b>	<b>35.42</b>	<b>31.88</b>	<b>34.91</b>	<b>32.96</b>

**NOTE 14 – DIVIDENDS PER SHARE**

During 2007, dividends were granted from retained earnings of previous years in the amount of HRK 29,017 thousand (2006: HRK 29,017 thousand), which amounts to HRK 12.65 per share (2006: HRK 12.65 per share). Dividend per share was calculated based on issued shares less treasury shares at the time the dividend was declared.

Unpaid dividends for 2007 in the amount of HRK 1,312 thousand (2006: HRK 15,687 thousand) are included as dividends payable in "trade and other payables" (Note 28).

According to a loan agreement concluded between the Company and one of its banks (Note 27), dividends are restricted to 50% of net profit for any year during the term of the loan agreement.

## NOTE 15 – INTANGIBLE ASSETS

**Group***(in thousands of HRK)*

	<u>Goodwill</u>	<u>Software</u>	<u>Total</u>
<b>At 31 December 2005</b>			
Cost	-	9,095	9,095
Accumulated amortisation	-	(3,127)	(3,127)
<b>Net book amount</b>	<b>-</b>	<b>5,968</b>	<b>5,968</b>
<b>Year ended 31 December 2006</b>			
Opening net book amount	-	5,968	5,968
Additions	-	4,707	4,707
Amortisation	-	(978)	(978)
Closing net book amount	-	9,697	9,697
<b>At 31 December 2006</b>			
Cost	-	13,802	13,802
Accumulated amortisation	-	(4,105)	(4,105)
<b>Net book amount</b>	<b>-</b>	<b>9,697</b>	<b>9,697</b>
<b>Year ended 31 December 2007</b>			
Opening net book amount	-	9,697	9,697
Acquisition of subsidiary (Note 30)	3,326	-	3,326
Additions	-	10,823	10,823
Amortisation	-	(1,141)	(1,141)
Closing net book amount	3,326	19,379	22,705
<b>At 31 December 2007</b>			
Cost	3,326	24,625	27,951
Accumulated amortisation	-	(5,246)	(5,246)
<b>Net book amount</b>	<b>3,326</b>	<b>19,379</b>	<b>22,705</b>

## NOTE 15 – INTANGIBLE ASSETS (continued)

**Company***(in thousands of HRK)*

	<u>Software</u>
<b>At 31 December 2005</b>	
Cost	9,095
Accumulated amortisation	(3,127)
<b>Net book amount</b>	<b>5,968</b>
<b>Year ended 31 December 2006</b>	
Opening net book amount	5,968
Additions	4,707
Amortisation	(978)
Closing net book amount	9,697
<b>At 31 December 2006</b>	
Cost	13,802
Accumulated amortisation	(4,105)
<b>Net book amount</b>	<b>9,697</b>
<b>Year ended 31 December 2007</b>	
Opening net book amount	9,697
Additions	10,823
Amortisation	(1,141)
Closing net book amount	19,379
<b>At 31 December 2007</b>	
Cost	24,625
Accumulated amortisation	(5,246)
<b>Net book amount</b>	<b>19,379</b>

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 16 – PROPERTY, PLANT AND EQUIPMENT

<b>Group</b>					
<i>(in thousands of HRK)</i>	<b>Land</b>	<b>Buildings</b>	<b>Equipment</b>	<b>Work in progress</b>	<b>Total</b>
<b>At 31 December 2005</b>					
Cost	36,871	316,561	373,913	2,440	729,785
Accumulated depreciation	-	(165,576)	(214,202)	-	(379,778)
<b>Net book amount</b>	<b>36,871</b>	<b>150,985</b>	<b>159,711</b>	<b>2,440</b>	<b>350,007</b>
<b>Year ended 31 December 2006</b>					
At 1 January	36,871	150,985	159,711	2,440	350,007
Additions	-	-	-	97,133	97,133
Transfers	8,992	28,944	55,805	(93,741)	-
Disposals	-	(21)	(845)	-	(866)
Exchange differences	(12)	111	115	-	214
Depreciation	-	(6,476)	(28,379)	-	(34,855)
At 31 December	45,851	173,543	186,407	5,832	411,633
<b>At 31 December 2006</b>					
Cost	45,851	345,574	423,266	5,832	820,523
Accumulated depreciation	-	(172,031)	(236,859)	-	(408,890)
<b>Net book amount</b>	<b>45,851</b>	<b>173,543</b>	<b>186,407</b>	<b>5,832</b>	<b>411,633</b>
<b>Year ended 31 December 2007</b>					
At 1 January	45,851	173,543	186,407	5,832	411,633
Additions	-	-	-	105,845	105,845
Transfers	134	39,125	53,274	(92,533)	-
Acquisition of TIM d.d. Topusko (Note 30)	954	22,999	1,515	-	25,468
Disposals	-	(22)	(2,459)	-	(2,481)
Exchange differences	11	36	77	-	124
Depreciation	-	(7,645)	(34,437)	-	(42,082)
At 31 December	46,950	228,036	204,377	19,144	498,507
<b>At 31 December 2007</b>					
Cost	46,950	407,698	478,055	19,144	951,847
Accumulated depreciation	-	(179,662)	(273,678)	-	(453,340)
<b>Net book amount</b>	<b>46,950</b>	<b>228,036</b>	<b>204,377</b>	<b>19,144</b>	<b>498,507</b>

As at 31 December 2007, the Group's advances for property, plant and equipment amounted to HRK 129 thousand (2006: HRK 1,273 thousand).

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 16 – PROPERTY, PLANT AND EQUIPMENT (continued)

## Company

*(in thousands of HRK)*

	Land	Buildings	Equipmen t	Work in progress	Total
<b>At 31 December 2005</b>					
Cost	16,316	167,879	308,293	297	492,785
Accumulated depreciation	-	(118,209)	(164,799)	-	(283,008)
<b>Net book amount</b>	<b>16,316</b>	<b>49,670</b>	<b>143,494</b>	<b>297</b>	<b>209,777</b>
<b>Year ended 31 December 2006</b>					
At 1 January	16,316	49,670	143,494	297	209,777
Transfer to investment property (Note 17)	(28)	-	-	-	(28)
Additions	-	23,193	44,434	3,822	71,449
Disposals	-	(21)	(813)	-	(834)
Depreciation	-	(3,856)	(25,568)	-	(29,424)
At 31 December	16,288	68,986	161,547	4,119	250,940
<b>At 31 December 2006</b>					
Cost	16,288	190,366	343,874	4,119	554,647
Accumulated depreciation	-	(121,380)	(182,327)	-	(303,707)
<b>Net book amount</b>	<b>16,288</b>	<b>68,986</b>	<b>161,547</b>	<b>4,119</b>	<b>250,940</b>
<b>Year ended 31 December 2007</b>					
At 1 January	16,288	68,986	161,547	4,119	250,940
Transfer to investment property (Note 17)	(2,901)	-	-	-	(2,901)
Additions	134	13,860	41,787	13,715	69,496
Disposals	-	-	(2,175)	-	(2,175)
Depreciation	-	(4,491)	(29,364)	-	(33,855)
At 31 December	13,521	78,355	171,795	17,834	281,505
<b>At 31 December 2007</b>					
Cost	13,521	204,226	375,476	17,384	611,058
Accumulated depreciation	-	(125,871)	(203,681)	-	(329,553)
<b>Net book amount</b>	<b>13,521</b>	<b>78,355</b>	<b>171,795</b>	<b>17,834</b>	<b>281,505</b>

As at 31 December 2007, the Company's advances for property, plant and equipment amounted to HRK 46 thousand (2006: HRK 1,273 thousand).

As at 31 December 2007, land, buildings and equipment of the Group and the Company with a net book value of HRK 102,989 thousand (2006: HRK 98,804 thousand) were pledged as security for borrowings received (Note 27).

As at 31 December 2007, assets leased under finance leases where the Group and the Company are the lessee amounted to HRK 1,431 thousand (2006: HRK 3,400 thousand) – see Note 27.

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 17 – INVESTMENT PROPERTY

*(in thousands of HRK)*

	<u>Land</u>	<u>Buildings</u>	<u>Total</u>
<b>As at 31 December 2005</b>			
Cost	12,869	82,089	94,958
Accumulated depreciation	-	(3,830)	(3,830)
<b>Net book amount</b>	<b><u>12,869</u></b>	<b><u>78,259</u></b>	<b><u>91,128</u></b>
<b>Year ended 31 December 2006</b>			
As at 1 January	12,869	78,259	91,128
Transfer from property, plant and equipment (Note 16)	28	-	28
Additions	8,816	553	9,369
Depreciation	-	(2,184)	(2,184)
As at 31 December	<u>21,713</u>	<u>76,628</u>	<u>98,341</u>
<b>As at 31 December 2006</b>			
Cost	21,713	82,628	104,341
Accumulated depreciation	-	(6,000)	(6,000)
<b>Net book amount</b>	<b><u>21,713</u></b>	<b><u>76,628</u></b>	<b><u>98,341</u></b>
<b>Year ended 31 December 2007</b>			
As at 1 January	21,713	76,628	98,341
Transfer from property, plant and equipment (Note 16)	2,901	-	2,901
Additions	-	22,962	22,962
Depreciation	-	(2,201)	(2,201)
As at 31 December	<u>24,614</u>	<u>97,389</u>	<u>122,003</u>
<b>As at 31 December 2007</b>			
Cost	24,614	105,590	130,204
Accumulated depreciation	-	(8,201)	(8,201)
<b>Net book amount</b>	<b><u>24,614</u></b>	<b><u>97,389</u></b>	<b><u>122,003</u></b>

Based on the current market prices and location of the property, Management determined that the fair value of investment property approximates its carrying amount.

All land and buildings have been pledged as security for borrowings received (Note 27).

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 18 – INVESTMENTS IN SUBSIDIARIES

	Dalekovod Group		Dalekovod d.d.	
	2007	2006	2007	2006
At 1 January	253	225	31,076	28,228
Additions	20	28	29,567	2,848
At 31 December	<b>273</b>	<b>253</b>	<b>60,643</b>	<b>31,076</b>

The principal subsidiary undertakings at 31 December are as follows:

Name	Country of incorporation	2007	2006	2007	2006
		<i>Holding in %</i>		<i>(in thousands of HRK)</i>	
Dalekovod d.o.o., Ljubljana	Slovenia	100.00	100.00	2,075	2,075
Dalekovod d.o.o., Mostar	Bosnia and Herzegovina	100.00	100.00	210	210
Dalekovod-Cinčaonica d.o.o., Dugo Selo	Croatia	100.00	100.00	1,000	1,000
Dalekovod-projekt d.o.o., Zagreb	Croatia	100.00	100.00	25	25
Dalcom Engineering GmbH, Freilassing	Germany	100.00	100.00	372	372
Dalekovod-Polska S.A., Warsaw	Poland	95.00	95.00	2,597	2,597
Dalekovod TKS a.d., Doboj	Bosnia and Herzegovina	83.17	83.17	11,934	11,934
Unidal d.o.o., Vinkovci	Croatia	50.54	50.54	16,185	12,635
Dalekovod ESOP d.o.o., Zagreb	Croatia	100.00	100.00	200	200
Denacco Namibia (PTY) Ltd	Namibia	60.00	60.00	18	18
Zablaće d.o.o., Zagreb	Croatia	-	50.00	-	10
Dalekovod TIM Topusko d.d.	Croatia	88.83	-	25,997	-
Dalekovod – ulaganje d.o.o. Zagreb	Croatia	100.00	-	20	-
Dalekovod EKO d.o.o. Zagreb	Croatia	50.00	-	10	-
				<b>60,643</b>	<b>31,076</b>

At the end of 2007, a capital contribution in Unidal d.o.o. Vinkovci was performed in the total amount of HRK 7,024 thousand. Each of the owners participated based on the proportion of the shares held: The minority owner paid in HRK 3,474 thousand, and the Company paid in HRK 3,550 thousand.

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 18 – INVESTMENTS IN SUBSIDIARIES (continued)

Subsidiaries not included in consolidation as at 31 December are as follows:

Name	Country of incorporation	2007	2006	2007	2006
		Holding in %		(in thousands of HRK)	
Dalekovod-projekt d.o.o., Zagreb	Croatia	100.00	100.00	25	25
Dalekovod ESOP d.o.o.	Croatia	100.00	100.00	200	200
Denacco Namibia (PTY) Ltd	Namibia	60.00	60.00	18	18
Zablaće d.o.o., Zagreb (Note 19)	Croatia	-	50.00	-	10
Dalekovod – ulaganje d.o.o. Zagreb	Croatia	100.00	-	20	-
Dalekovod EKO d.o.o. Zagreb	Croatia	50.00	-	10	-
				<b>273</b>	<b>253</b>

Subsidiaries Dalekovod ESOP, Dalekovod-projekt, Dalekovod – Ulaganje and Dalekovod –EKO do not perform any operating activities and therefore are not included in consolidation.

## NOTE 19 – AVAILABLE-FOR-SALE FINANCIAL ASSETS

(in thousands of HRK)	Dalekovod Group		Dalekovod d.d.	
	2007	2006	2007	2006
At beginning of year	7,485	6,746	7,485	6,746
Transfer from investments	10	-	10	-
Additional investments	14,876	739	14,876	739
Fair value adjustment	5,064	-	5,064	-
At end of year	<b>27,435</b>	<b>7,485</b>	<b>27,435</b>	<b>7,485</b>

The Company owns 8.57% of shares in a closed-ended investment fund. On behalf of the Company, this fund acquires shares in domestic companies, with the purpose of developing such companies and improving their long-term market position, as well as realising future benefits for the investors. During the year, the Company invested an additional amount of HRK 7,666 thousand in the fund.

In November 2006, the Company and two other domestic companies established the subsidiary Zablaće d.o.o., Zagreb. The Company paid in HRK 10 thousand of the founding capital, which represented 50% of interest in the newly established company. In 2007, all owners performed a capital contribution, and the Company invested an additional amount of HRK 7,210 thousand and decreased its holding in the company (33%).

As at 31 December, the Company performed a valuation of its available-for-sale financial assets and adjusted them to fair value. The increase of HRK 5,064 thousand is recognised within revaluation reserves (Note 26).

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 20a – FINANCIAL INSTRUMENTS BY CATEGORY

The accounting policies for financial instruments have been applied to the line items below:

**Group**

*(in thousands of HRK)*

	<b>Note</b>	<b>Loans and receivables</b>	<b>Financial assets at fair value through profit or loss</b>	<b>Available- for-sale financial assets</b>	<b>Total</b>
<b>31 December 2007</b>					
<b>Financial assets</b>					
Trade and other receivables	23	681,073	-	-	<b>681,073</b>
Loans and deposits given	21,23	124,032	-	-	<b>124,032</b>
Available-for-sale financial assets (changes through capital)	19	-	-	27,435	<b>27,435</b>
Financial assets at fair value through profit or loss	24	-	916	-	<b>916</b>
Cash and cash equivalents	25	186,211	-	-	<b>186,211</b>
<b>Total</b>		<b>991,316</b>	<b>916</b>	<b>27,435</b>	<b>1,019,667</b>

*(in thousands of HRK)*

	<b>Note</b>	<b>Other financial liabilities</b>
<b>31 December 2007</b>		
<b>Financial liabilities</b>		
Borrowings	27	535,516
Trade payables	28	443,941
Other payables	28	21,436
<b>Total</b>		<b>1,000,893</b>

Financial instruments do not include business transactions with employees, receivables/payables for contributions, taxes and receivables/payables for advances received.

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 20a – FINANCIAL INSTRUMENTS BY CATEGORY (continued)

## Group

(in thousands of HRK)

	Note	Loans and receivables	Financial assets at fair value through profit or loss	Available-for-sale financial assets	Total
<b>31 December 2006</b>					
<b>Financial assets</b>					
Trade and other receivables	23	500,936	-	-	<b>500,936</b>
Loans and deposits given	21,23	50,124	-	-	<b>50,124</b>
Available-for-sale financial assets (changes through capital)	19	-	-	7,485	<b>7,485</b>
Financial assets at fair value through profit or loss	24		6,687	-	<b>6,687</b>
Cash and cash equivalents	25	29,425	-	-	<b>29,425</b>
<b>Total</b>		<b>580,485</b>	<b>6,687</b>	<b>7,485</b>	<b>594,657</b>

(in thousands of HRK)

	Note	Other financial liabilities
<b>31 December 2006</b>		
<b>Financial liabilities</b>		
Borrowings	27	402,223
Trade payables	28	232,158
Other payables	28	20,710
<b>Total</b>		<b>655,091</b>

## NOTE 20b – CREDIT QUALITY OF FINANCIAL ASSETS

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.

	<u>2007</u>	<u>2006</u>
	<i>(in thousands of HRK)</i>	
<b>Trade receivables – neither past due nor impaired</b>		
Existing customers – payments within maturity period	146,144	145,055
Existing customers – with some defaults in the past	183,604	165,179
	<b>329,748</b>	<b>310,234</b>

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 20b – CREDIT QUALITY OF FINANCIAL ASSETS (continued)

The Group mainly deposits its cash with a bank with a BBB - credit rating by Standard & Poor's.

<b>Cash at bank and deposits</b>	<u>2007</u>	<u>2006</u>
	<i>(in thousands of HRK)</i>	
BBB -	172,349	17,183
Without rating	<u>13,862</u>	<u>12,062</u>
	<b>186,211</b>	<b>29,245</b>

## NOTE 21 – LOANS AND RECEIVABLES

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<u>2007</u>	<u>2006</u>	<u>2007</u>	<u>2006</u>
Long-term deposits	6,034	135	6,034	135
Long-term loans receivable:				
- consumer goods loan	18,341	25,256	17,952	25,256
- housing loans and other loans to employees	5,666	6,407	5,666	6,407
- ESOP (Employee Share Ownership Plan)	84	1,784	84	1,784
Total long-term loans and deposits	<u>30,125</u>	<u>33,582</u>	<u>29,736</u>	<u>33,582</u>
Current portion of long-term loans and deposits (Note 23)	<u>(8,363)</u>	<u>(18,815)</u>	<u>(8,363)</u>	<u>(18,815)</u>
<b>Long-term loans and deposits</b>	<b><u>21,762</u></b>	<b><u>14,767</u></b>	<b><u>21,373</u></b>	<b><u>14,767</u></b>

**Consumer goods loan**

Consumer goods loans represent trade receivables from customers in Bosnia and Herzegovina based on the sale of equipment and the provision of services, which were transformed into a loan repayable within a period of 2 years with an interest rate set at 4.5% p.a.

**Housing loans**

Housing loans to employees carry an average effective interest rate of 6%, and are repayable over 2 to 25 years through deductions from employee salaries. Housing loans are denominated in HRK with currency clauses (EURO).

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

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## NOTE 21 – LOANS AND RECEIVABLES (continued)

**ESOP loans receivable**

Under the ESOP plan, in 2000 and 2001, employees received a certain amount of shares at market prices at that time. At the same time, loans were granted to employees for the payment of these shares. The Company has first purchase right of shares when an employee leaves the Company for amounts not yet paid.

Loans to employees for the purchase of Company shares through the Employee Share Ownership Plan (ESOP) bear an annual interest of 6% and are repayable over 6 years in equal annual instalments. ESOP loans are denominated in HRK. During 2006, ESOP loans from 2000 have been repaid, while in 2007, the major portion of ESOP loans from 2001 was repaid.

As at 31 December 2007, loans to executive directors relating to the ESOP plan were fully repaid (2006: HRK 16 thousand). The loans were granted under conditions equal to those granted to other employees.

The fair value of long-term loans approximates their carrying amount, since loan interest rates reflect market rates.

**Deposits**

Deposits are denominated in HRK with currency clauses (EURO).

## NOTE 22 – INVENTORIES

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Raw materials	138,614	119,159	108,236	89,742
Finished goods, semi-finished goods and work in progress	118,198	72,613	112,177	68,552
Spare parts and small inventories	5,666	2,835	4,922	2,836
Trade goods	4,088	397	3,688	-
	<b>266,566</b>	<b>195,004</b>	<b>229,023</b>	<b>161,130</b>

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 23 – TRADE AND OTHER RECEIVABLES

<i>(in thousands of HRK)</i>	Dalekovod Group		Dalekovod d.d.	
	2007	2006	2007	2006
Domestic trade receivables	446,655	364,505	409,914	415,895
Foreign trade receivables	171,327	106,106	226,987	108,343
Provisions for impairment	(10,129)	(10,033)	(9,866)	(9,411)
	<b>607,853</b>	<b>460,578</b>	<b>627,035</b>	<b>514,827</b>
Receivable from customers for contract work	48,926	30,500	48,926	30,500
Retentions	72,068	3,326	72,068	3,326
Current portion of long-term loans (Note 19)	8,363	18,815	8,363	18,815
Loan to subsidiary (Note 32)	-	-	9,402	8,127
Other short-term loans	21,839	13,216	21,838	13,551
Advances	35,672	19,816	36,283	19,800
Receivable from employees	1,294	914	1,294	868
Other current assets	24,294	9,858	12,055	7,598
	<b>820,309</b>	<b>557,023</b>	<b>837,264</b>	<b>617,412</b>

Total construction costs incurred and recognised profits (less recognised losses to date) for all active construction contracts amounted to HRK 3,144,582 thousand (2006: HRK 3,796,338 thousand).

Other short-term loans and a loan to subsidiary represent primarily trade receivables converted to loans and loans given to sports organisations with annual interest rates from 3%-6%. The loans are generally granted for periods of 3 to 9 months and are secured by bills of exchange and promissory notes.

Advances were granted to suppliers for the purchase of material and equipment, as well as for project design services.

As at 31 December 2007, the Group recognised trade receivables in the amount of HRK 278,105 thousand (2006: HRK 150,344 thousand) that were past due, but not impaired. They mainly compose of receivables from customers owned by the state who have some defaults in payments. The ageing of these receivables is based on the number of days outstanding after the maturity date:

	2007	2006
	<i>(in thousands of HRK)</i>	
Up to 90 days	199,049	115,033
From 91 to 180 days	25,498	16,021
Over 180 days	53,558	19,290
	<b>278,105</b>	<b>150,344</b>

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 23 – TRADE AND OTHER RECEIVABLES (continued)

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

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
At 1 January	10,033	11,959	9,411	11,959
Provision for receivables impairment (Note 9)	800	839	588	209
Collected amounts (Note 9)	(364)	(708)	(50)	(708)
Receivables written off during the year as uncollectible	(340)	(2,057)	(83)	(2,049)
At 31 December	10,129	10,033	9,866	9,411

The carrying amounts of the Group's and the Company's trade and other receivables are denominated in the following currencies:

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
EUR	120,847	70,659	94,362	69,002
USD	124,990	39,341	124,990	39,341
HRK	574,472	447,023	617,912	509,069
Total	<b>820,309</b>	<b>557,023</b>	<b>837,264</b>	<b>617,412</b>

The maximum exposure to credit risk at the reporting date is the carrying value of each class of receivable mentioned above. The Group or the Company hold collaterals as security.

The fair value of trade receivables approximates their carrying amount.

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

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**NOTE 24 – FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS**

During 2007, the Group invested in domestic cash funds. As at 31 December 2007, fair value of these assets in the Group amounted to HRK 916 thousand, and in the Company HRK 894 thousand (2006: HRK 6,687 thousand). The change in fair value of HRK 123 thousand (2006: HRK 337 thousand) is recognized in the income statement as a fair value gain (Note 10).

**NOTE 25 – CASH AND CASH EQUIVALENTS**

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Domestic currency	18,699	5,476	10,568	4,095
Foreign currency	22,326	23,949	22,326	13,302
Short-term deposits at bank	145,186	-	144,601	-
	<b>186,211</b>	<b>29,425</b>	<b>177,495</b>	<b>17,397</b>

Depending on the availability of cash, the Company places short-term deposits (with maturities of three months or less) with various banks for the purpose of realising additional interest income.

As at 31 December 2007, the average effective interest rate for short-term deposits with banks was 7.6%.

**NOTE 26 – SHAREHOLDERS' EQUITY**

**Share capital**

As at 31 December 2007, the share capital of the Company consisted of 2,293,812 ordinary shares, authorised and issued, with a nominal value of HRK 100 per share. All issued shares are fully paid.

As at 31 December 2007 and 2006 the Company owns 24,828 treasury shares.

The structure of shareholders as at 31 December:

	<u>2007</u>	<u>2006</u>
Natural persons	28.55%	37.60%
BMK i Partneri d.o.o.	17.92%	18.24%
KLT i Partneri d.o.o.	17.86%	18.06%
CTG d.o.o.	16.83%	16.81%
Treasury shares	1.08%	1.08%
Other	17.76%	8.21%
	<u>100.00%</u>	<u>100.00%</u>

**Legal, statutory and other reserves**

The legal reserve is required under Croatian law and must be built up at a minimum of 5% of the profit for the year until the total legal reserve reaches 5% of the Company's share capital. Legal reserves are not distributable.

During 2007, according to the decision of the Annual General Meeting statutory reserves were increased by HRK 45,850 thousand (2006: HRK 43,374 thousand). These reserves are distributable.

Other reserves consist of profits from previous periods set aside by the decision of the General Meeting (these reserves are distributable) and treasury shares reserves. According to Croatian regulations, in earlier years reserves for treasury shares were formed in the amount of HRK 1,244 thousand.

**Revaluation reserves**

As at 31 December 2007, the Group and the Company performed a valuation of fair value of available-for-sale financial assets (shares and interests in the investment fund – Note 19) and, in accordance with the applicable accounting policy, an increase was performed in revaluation reserves in the amount of HRK 5,064 thousand.

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 27 – BORROWINGS

<i>(in thousands of HRK)</i>	Average interest rates	Dalekovod Group		Dalekovod d.d.	
		2007	2006	2007	2006
<b>Long-term</b>					
Bank borrowings	6.11%	194,090	181,762	173,796	172,105
Finance lease	7.27%	1,137	1,137	378	1,137
		<b>195,227</b>	<b>182,899</b>	<b>174,174</b>	<b>173,242</b>
<b>Short-term</b>					
Bank borrowings	6.29%	232,217	143,270	219,318	142,290
Commercial papers	4.49%	107,000	75,000	107,000	75,000
Finance lease		755	1,054	755	1,054
		<b>339,972</b>	<b>219,324</b>	<b>327,073</b>	<b>218,344</b>
<b>Total borrowings</b>		<b>535,199</b>	<b>402,223</b>	<b>501,247</b>	<b>391,586</b>

Under the terms of a loan agreement concluded between the Company and one of its banks, the Company is obliged to maintain specific financial and non-financial restrictions (covenants). The covenants include conditions on the payment of dividends (Note 14), and the maintenance of financial covenants including: debt to equity, sale of assets, overdue payables and debt service coverage. As at 31 December 2007, all above stated covenants have been met.

During 2007, the Company issued commercial papers in the amount of HRK 32 million in denominations of HRK 1.00 for a period of 364 days from the day of issuance with a nominal yield of 4.13% p.a.

The bank borrowings are secured with bills of exchange and by mortgage over property, plant and equipment and investment property (Note 16).

As at 31 December 2007, interest payable on long-term and short-term borrowings amounted to HRK 4,843 thousand (2006: HRK 4,152 thousand), (Note 28).

The Group's borrowings in the amount of HRK 403,562 thousand (2006: HRK 326,875 thousand) are exposed to interest rate changes, since the contracted interest rate is variable. Other borrowings have fixed interest rates and are exposed to interest rate changes upon maturity of the principal.

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 27 – BORROWINGS (continued)

The exposure of the borrowings to interest rate changes at the balance sheet date is as follows (other borrowings are stated at fixed rates):

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
3 months	248,103	170,945	241,303	170,945
6 months	40,104	40,575	21,426	28,095
12 months	10,000	10,000	10,000	10,000
5 years	105,355	105,355	97,305	105,355
	<b>403,562</b>	<b>326,875</b>	<b>370,034</b>	<b>314,395</b>

The carrying amount of the Group's long-term borrowings approximates their fair value, since the stated interest rates reflect current market interest rates.

Principal repayments on long-term borrowings and financial lease are as follows:

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Loans in use	48,710	25,922	45,065	25,922
Between 1 and 2 years	48,494	27,430	37,978	24,492
Between 2 and 5 years	58,380	75,340	51,488	68,621
Over 5 years	39,643	54,207	39,643	54,207
	<b>195,227</b>	<b>182,899</b>	<b>174,174</b>	<b>173,242</b>

The borrowings are denominated in the following currencies:

	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
EUR	251,590	95,808	232,912	86,309
CHF	6,800	-	-	-
HRK	276,809	306,415	268,335	305,277
	<b>535,199</b>	<b>402,223</b>	<b>501,247</b>	<b>391,586</b>

Borrowings with currency clauses are included in HRK borrowings.

The Group and the Company have the following undrawn borrowing facilities:

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Expiring within one year at: - floating rate	48,166	48,166	9,828	48,166
	<b>48,166</b>	<b>48,166</b>	<b>9,828</b>	<b>48,166</b>

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 28 – TRADE AND OTHER PAYABLES

<i>(in thousands of HRK)</i>	Dalekovod Group		Dalekovod d.d.	
	2007	2006	2007	2006
Domestic suppliers	318,286	177,658	299,861	209,723
Foreign suppliers	125,655	54,500	136,653	33,879
	<b>443,941</b>	<b>232,158</b>	<b>436,514</b>	<b>243,602</b>
Advances received for construction work	176,158	16,180	176,158	16,180
Advances	52,793	7,770	53,065	4,041
Salaries	16,532	12,678	14,125	10,427
Taxes and contributions on and from salaries	12,008	11,875	10,551	10,403
Dividend payable (Note 14)	1,312	15,687	1,312	15,687
Interest payable	4,843	4,152	4,490	4,098
VAT payable	25,865	15,557	30,843	17,782
Other accruals and liabilities	16,593	16,558	11,693	15,427
	<b>750,045</b>	<b>332,615</b>	<b>738,751</b>	<b>337,647</b>

The dividend payable represents unpaid dividend declared in respect of prior periods.

## NOTE 29 – PROVISIONS

<i>(in thousands of HRK)</i>	Jubilee awards	Retirement severance payment	Total
At 1 January 2007	4,552	2,721	7,273
Reversal of provision	(133)	(239)	(372)
Used during the period	(329)	(32)	(361)
<b>At 31 December 2007</b>	<b>4,090</b>	<b>2,450</b>	<b>6,540</b>

*Retirement severance payment*

According to the Collective bargaining agreement the Group has an obligation to make severance payments to employees at the time of the employees' retirement. The liability is calculated by independent actuaries. Significant assumptions used by the actuary are as follows: an annual leaver's rate of 0,88%, an annual discount rate of 5,4%; the age of retirement is determined for each individual employee taking into account their present age and the overall realised years of service (the average age of retirement used in the calculation is 62 years for men and 58 years for women).

*Jubilee awards*

This provision relates to estimated long-term employee benefits (jubilee awards) as defined in the Collective bargaining agreement.

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

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## NOTE 30 – ACQUISITION

In February 2007, the Group acquired an 88.83% interest in the company Tvornica istegnutih metala d.d., Topusko (TIM d.d., Topusko), specialised for production of expanded metals and fences. The acquired company contributed revenues of HRK 30,616 thousand and net profit of HRK 513 thousand to the consolidated result for the year ended 31 December 2007. If the acquisition had occurred on 1 January 2007, the consolidated revenues for the year ended 31 December 2007 would have been HRK 2,271 thousand higher, while the profit before tax would have been HRK 1,040 thousand lower than the one realised.

Details of net assets and goodwill are as follows:

Purchase consideration	25,997
Fair value of net assets acquired	<u>(22,651)</u>
Goodwill	3,346

The assets and liabilities as at 31 December 2006 arising from the acquisition are as follows:

<i>(in thousands of HRK)</i>	<u>Carrying amount</u>	<u>Fair value</u>
Cash	2,220	2,220
Tangible assets	11,686	25,468
Inventories	9,537	9,537
Trade and other receivables	9,621	9,530
Trade and other payables	(8,318)	(8,318)
Borrowings	<u>(12,938)</u>	<u>(12,938)</u>
<b>Net assets</b>	<b>11,808</b>	<b>25,499</b>
Minority interests (11.17%)		<u>(2,848)</u>
<b>Net assets acquired</b>		<b>22,651</b>

Purchase consideration settled in cash	25,997
Cash and cash equivalents acquired	<u>(2,220)</u>
Cash outflow on acquisition	23,777

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 31 – CASH GENERATED FROM OPERATIONS

<i>(in thousands of HRK)</i>	<u>Note</u>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
		<u>2007</u>	<u>2006</u>	<u>2007</u>	<u>2006</u>
Profit before tax		101,811	94,321	100,762	97,742
Adjustments for:					
Depreciation and amortisation		42,082	35,833	37,197	32,586
Unrealised foreign exchange differences		(3,028)	(1,620)	(7,394)	(773)
Property, plant and equipment written off		2,473	220	2,175	221
Provision for trade receivables		800	839	588	209
Provision for inventories		247	551	160	551
Provision for long-term employee benefits		(733)	7,273	(733)	7,273
Impairment of loans given		-	2,441	-	2,441
Loss/(gain) on sale of property, plant and equipment		(650)	6	(524)	(239)
Minority interest	18, 30	6,322	-	-	-
Fair value gains		(123)	(337)	(123)	(337)
Interest income		(6,723)	(3,425)	(5,707)	(3,477)
Interest expense		25,228	19,084	22,278	18,571
Other		-	-	-	(707)
		<u>65,895</u>	<u>60,865</u>	<u>47,917</u>	<u>56,319</u>
Changes in working capital:					
Trade and other receivables		(191,990)	(128,773)	(147,318)	(156,369)
Inventories		(62,272)	(33,205)	(68,053)	(13,350)
Trade and other payables		<u>428,225</u>	<u>30,885</u>	<u>402,779</u>	<u>34,026</u>
<b>Net cash generated from operations</b>		<b><u>341,669</u></b>	<b><u>24,093</u></b>	<b><u>336,087</u></b>	<b><u>18,368</u></b>

In the cash flow statement, proceeds from the sale of property, plant and equipment comprise:

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<u>2007</u>	<u>2006</u>	<u>2007</u>	<u>2006</u>
Net book amount	2,473	859	2,175	613
Net (loss)/gain on sale of property, plant and equipment (Note 10)	<u>650</u>	<u>(6)</u>	<u>524</u>	<u>239</u>
Proceeds from sale of property, plant and equipment	<b><u>3,123</u></b>	<b><u>853</u></b>	<b><u>2,699</u></b>	<b><u>852</u></b>

## NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2007

## NOTE 32 – RELATED PARTY TRANSACTIONS

In the ordinary course of business operations, the Company enters into related party transactions, which include the purchase of goods and services and loans. In addition to the subsidiaries presented in Note 18, the Company's related parties include its Management Board and executive directors.

*Year-end balances resulting from transactions with subsidiaries are as follows:*

**Revenues and expenses**

	<u>2007</u>	<u>2006</u>
	<i>(in thousands of HRK)</i>	
Sales	143,753	61,687
Rental income	15,540	14,681
Sale of properties	-	673
	<u>159,293</u>	<u>77,041</u>
Cost of materials and services	31,456	25,076
Subcontractor services	103,451	48,620
Other operating expenses	1,808	2,259
	<u>136,715</u>	<u>75,955</u>

**Receivables, payables and loans**

	<u>2007</u>	<u>2006</u>
	<i>(in thousands of HRK)</i>	
Trade receivables	76,793	65,614
Other receivables	1,105	-
Short-term loans given	9,402	8,127
		<u>73,741</u>
Trade payables	76,599	24,652
	<u>76,599</u>	<u>24,652</u>

*Year-end balances resulting from transactions with key management are as follows:*

<i>(in thousands of HRK)</i>	<b>Dalekovod Group</b>		<b>Dalekovod d.d.</b>	
	<u>2007</u>	<u>2006</u>	<u>2007</u>	<u>2006</u>
<b>Revenues and expenses</b>				
Net salaries	8,834	9,074	7,189	7,850
Contributions	3,932	4,220	3,342	3,530
	<u>12,766</u>	<u>13,294</u>	<u>10,531</u>	<u>11,380</u>
Interest income	41	45	36	40
<b>Loans</b>				
ESOP and housing loans	1,045	943	1,045	943

**NOTE 33 – CONTINGENCIES AND COMMITMENTS**

As at 31 December 2007, the Group has numerous contracts for the provision of construction services which require future costs to be incurred. Costs to be incurred in the future arising from these contracts are estimated in the amount of HRK 2,231,398 thousand (2006: HRK 674,831 thousand). The Group guarantees adhering to deadlines and ensures quality for all work performed.

In the ordinary course of operations, the Group was plaintiff and defendant in several legal disputes. Management and legal counsel believe that these legal disputes will not result in significant losses.