

04

Financial Statements of  
Ericsson Nikola  
Tesla d.d.





Ericsson Nikola Tesla d.d.

# Company profile

## History and incorporation

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

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

According to the ownership structure as at 31 December 2017, Telefonaktiebolaget LM Ericsson (Ericsson) holds 49.07% of the Company's shares. Other shareholders own the remaining 50.91% of the Company's shares and 0.02% is held as treasury shares.

## Principal activities

The principal activities of the Company are research and development of telecommunications software and services, design, testing and integration of total communications solutions, and supply and maintenance of communications solutions and systems towards customers within the Ericsson Group, customers in the Republic of Croatia, and Bosnia and Herzegovina, and several customers in Central and Eastern Europe.

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

## Code of Corporate Governance

The Company applies the Code of Corporate Governance of the Zagreb Stock Exchange and meets the obligations derived therefrom, with the exception of provisions whose application is not practical at the moment.

## Supervisory Board, Audit Committee, Management Board and executive management

### Supervisory Board

The Supervisory Board members during 2017 and up to the release of these statements were:

|                    |                                     |                                      |
|--------------------|-------------------------------------|--------------------------------------|
| Arun Bansal        | Appointed on 6 June 2017            | Chairman                             |
| Roland Nordgren    | Resigned as chairman on 6 June 2017 |                                      |
| Ignac Lovrek       | Reappointed on 2 June 2015          | Member; Vice-Chairman                |
| Vidar Mohammar     | Appointed on 2 June 2015            | Member                               |
| Dubravko Radošević | Reappointed on 27 May 2014          | Member                               |
| Zvonimir Jelić     | Reappointed on 8 July 2014          | Member and employees' representative |

### Audit Committee

The Audit Committee members during 2017 and up to the release of these consolidated statements were:

|                |                               |          |
|----------------|-------------------------------|----------|
| Ignac Lovrek   | Reappointed on 2 June 2015    | Chairmen |
| Vidar Mohammar | Appointed on 3 September 2015 | Member   |
| Vesna Vašiček  | Appointed on 21 February 2017 | Member   |

Ericsson Nikola Tesla d.d.

# Company profile (continued)

## Supervisory Board, Audit Committee, Management Board and executive management (continued)

### Management Board

The Management Board has one member:

|                   |                               |           |
|-------------------|-------------------------------|-----------|
| Gordana Kovačević | Reappointed on 1 January 2015 | President |
|-------------------|-------------------------------|-----------|

### Executive management

As at 31 December 2017, the Company's executive management comprised:

|                          |   |
|--------------------------|---|
| Gordana Kovačević        | Company President   |
| Branko Dronjić           | Director, IT&Test Environment Operations                              |
| Damir Bušić              | Director, Commercial Management (including Legal)                     |
| Dario Runje              | Director, Networks  |
| Darko Huljenić           | Director, Research  |
| Dragan Fratrić           | Director, General Services  |
| Goran Ožbolt             | Director, Sales and Marketing for Tele2 and Alternative Operators     |
| Hrvoje Benčić            | Director, Digital Services and Operations                             |
| Ivan Barać               | Director, Sales and Marketing for Hrvatski Telekom and CIS Market     |
| Jagoda Barać             | Director, Sales and Marketing for Neighboring Countries               |
| Luciano Barreto Ferreira | Director, Finance (including Sourcing)                                |
| Marijana Đuzel           | Director, Human Resources   |
| Milan Živković           | Director, Strategy and Business Development                           |
| Miroslav Kantolić        | Director, Sales and Marketing for VIPnet                              |
| Patrick Gerard Martin    | Director, R&D Center  |
| Snježana Bahtijari       | Director, Marketing, Communications & Corporate Social Responsibility |

Ericsson Nikola Tesla d.d.

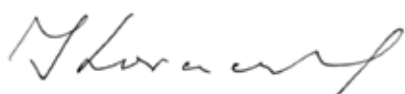
# Responsibilities of the Management and Supervisory Boards for the preparation and approval of the annual financial statements

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

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

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

The financial statements set out on pages 180 to 227 were authorised by the Management Board on 25 April 2018 for issue to the Supervisory Board and are signed below.



**Gordana Kovačević**

President

Ericsson Nikola Tesla d.d.

Krapinska 45

10000 Zagreb

Croatia





## Independent Auditor's Report

### To the Shareholders and Management Board of Ericsson Nikola Tesla d.d.:

## Report on the audit of the separate financial statements

### Our opinion

In our opinion, the separate financial statements present fairly, in all material respects, the financial position of Ericsson Nikola Tesla d.d. (the "Company") as at 31 December 2017, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union ("IFRS").

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

### What we have audited

The Company's separate financial statements comprise:

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

### Basis for opinion

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

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

### Independence

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

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

The non-audit services that we have provided to the Company, in the period from 1 January 2017 to 31 December 2017, are disclosed in the note 5 to the separate financial statements.

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## *Our audit approach*

### Overview

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|                          |   |
|--------------------------|---|
| <b>Materiality</b>       | <ul style="list-style-type: none"> <li>Overall materiality for separate financial statements as a whole: HRK 11.7 million, which represents 0.8% of sales revenue.</li> </ul> |
| <b>Key audit matters</b> | <ul style="list-style-type: none"> <li>Revenue recognition from sale of goods</li> </ul>  |

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### How we tailored our audit scope

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

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

### Materiality

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

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



**Overall materiality for separate financial statements as a whole**

HRK 11.7 million

**How we determined it**

0.8% of sales revenue

**Rationale for the materiality benchmark applied**

We consider revenue to be the benchmark against which the performance of the Company is most commonly measured by the shareholders. In addition, majority of the sales and purchases are realised from internal Ericsson Group transactions and are subject to transfer pricing arrangements.

**Key audit matters**

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

| Key audit matter   | How our audit addressed the Key audit matter  |
|--|---|
| <p><i>Recognition of revenue from sale of goods</i><br/>Refer to Note 1 of the financial statements under heading "Recognition of revenues" and Note 25 (Accrued charges and deferred revenue).</p> <p>We focused on revenue recognition because the customer payments set in the contracts usually do not align with timing of revenue recognition criteria. Revenue from delivery of goods is mostly recognised upon approved acceptance test by a customer.</p> | <p>We assessed the consistency of the application of the revenue recognition policy by performing following procedures:</p> <ul style="list-style-type: none"> <li>- We tested the design and operating effectiveness of the controls (including IT controls) over revenue systems across the Company to determine the extent of reliance on the automated controls and overall IT environment.</li> <li>- We checked that revenue had been recognised at the correct time by testing a sample of transactions and contracts, and comparing the timing of revenue recognition to approved client acceptance tests.</li> <li>- We also tested on a sample basis the appropriateness of deferred revenue transactions by reference to the delivery status of the related contracts and timing of invoices.</li> <li>- We verified appropriate allocation of revenue among multiple performance obligations for a selected number of contracts by analysing reasonableness of margins.</li> <li>- We also discussed with management the status of customer contracts not yet finalised to identify any unrecognized loss provisions. Based on discussion with responsible project managers, we assessed the reasonableness of expected costs for these contracts in comparison to actual costs.</li> </ul> <p>No exceptions were noted from our testing.</p> |





### *Reporting on other information including the Management report and Corporate Governance Statement*

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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## Report on other legal and regulatory requirements

### *Appointment*

We were first appointed as auditors of the Company on 26 May 2009 . Our appointment has been renewed annually by shareholder resolution representing a total period of uninterrupted engagement appointment of 9 years.

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The engagement partner on the audit resulting in this independent auditor's report is Tamara Maćašović.

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

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

Ericsson Nikola Tesla d.d.

# Statement of comprehensive income

for the year ended 31 December 2017

|  |       | 2017           | 2016           |
|--|-------|----------------|----------------|
|  | Notes | HRK '000       | HRK '000       |
| Sales revenue                                  | 3, 4  | 1,464,878      | 1,575,862      |
| Cost of sales                                  |       | (1,320,147)    | (1,389,129)    |
| <b>Gross profit</b>                            |       | <b>144,731</b> | <b>186,733</b> |
| Selling expenses                               |       | (44,847)       | (43,420)       |
| Administrative expenses                        |       | (33,103)       | (32,525)       |
| Other operating income                         |       | 7,511          | 4,809          |
| Other operating expenses                       |       | (3,070)        | (3,179)        |
| <b>Operating profit</b>                        |       | <b>71,222</b>  | <b>112,418</b> |
| Finance expense/income - net                   | 7     | (2,715)        | 5,250          |
| <b>Profit before tax</b>                       |       | <b>68,507</b>  | <b>117,668</b> |
| Income tax                                     | 8     | (4,224)        | (8,101)        |
| <b>Profit for the year</b>                     |       | <b>64,283</b>  | <b>109,567</b> |
| Other comprehensive income                     |       | -              | -              |
| <b>Total comprehensive income for the year</b> |       | <b>64,283</b>  | <b>109,567</b> |
| Earnings per share (HRK)                       | 9     | 48.32          | 82.45          |

Ericsson Nikola Tesla d.d.

# Statement of financial position

as at 31 December 2017

| Assets  | Notes  | 2017           | 2016           |
|---|--------|----------------|----------------|
|   |        | HRK '000       | HRK '000       |
| <b>Non-current assets</b>                             |        |                |                |
| Property, plant and equipment                         | 10     | 98,011         | 107,933        |
| Intangible assets                                     | 11     | 1,287          | 1,912          |
| Loans and receivables                                 | 12     | 82,874         | 81,160         |
| Investments in subsidiaries                           | 13     | 1,093          | 73             |
| Deferred tax assets                                   | 8      | 14,336         | 13,558         |
| <b>Total non-current assets</b>                       |        | <b>197,601</b> | <b>204,636</b> |
| <b>Current assets</b>                                 |        |                |                |
| Inventories   | 14     | 17,348         | 9,188          |
| Trade receivables                                     | 15     | 140,802        | 173,363        |
| Receivables from related parties                      | 26 (c) | 186,857        | 90,141         |
| Other receivables                                     | 16     | 17,575         | 14,040         |
| Financial assets at fair value through profit or loss | 17     | 84,520         | 62,993         |
| Prepayments and accrued income                        |        | 5,068          | 4,422          |
| Cash and cash equivalents                             | 18     | 145,086        | 213,375        |
| <b>Total current assets</b>                           |        | <b>597,256</b> | <b>567,522</b> |
| <b>Total assets</b>                                   |        | <b>794,857</b> | <b>772,158</b> |

Ericsson Nikola Tesla d.d.

# Statement of financial position (continued)

as at 31 December 2017

|                                      |        | 2017     | 2016     |
|--------------------------------------|--------|----------|----------|
| Equity and liabilities               | Notes  | HRK '000 | HRK '000 |
| <b>Equity</b>                        |        |          |          |
| Share capital                        | 19 (a) | 133,165  | 133,165  |
| Treasury shares                      |        | (280)    | (1,630)  |
| Legal reserves                       | 19 (c) | 6,658    | 6,658    |
| Retained earnings                    |        | 83,913   | 140,057  |
| <b>Total equity</b>                  |        | 223,456  | 278,250  |
| <b>Non-current liabilities</b>       |        |          |          |
| Borrowings                           | 20     | 8,378    | 8,954    |
| Employee benefits                    | 22 (a) | 5,279    | 5,487    |
| Other non-current liabilities        | 21     | 6,843    | 9,946    |
| <b>Total non-current liabilities</b> |        | 20,500   | 24,387   |
| <b>Current liabilities</b>           |        |          |          |
| Payables to related parties          | 26 (c) | 135,508  | 96,211   |
| Trade and other payables             | 23     | 197,123  | 130,460  |
| Income tax payable                   |        | 340      | 21,658   |
| Provisions                           | 24     | 26,619   | 15,967   |
| Accrued charges and deferred revenue | 25     | 191,311  | 205,225  |
| <b>Total current liabilities</b>     |        | 550,901  | 469,521  |
| <b>Total liabilities</b>             |        | 571,401  | 493,908  |
| <b>Total equity and liabilities</b>  |        | 794,857  | 772,158  |

Ericsson Nikola Tesla d.d.

# Statement of changes in equity

for the year ended 31 December 2017

|  | Share capital<br>HRK '000 | Treasury shares<br>HRK '000<br>Note 19 (b) | Legal reserves<br>HRK '000 | Retained earnings<br>HRK '000 | Total<br>HRK '000 |
|--|---------------------------|--|----------------------------|-------------------------------|-------------------|
| <b>As at 1 January 2016</b>  | 133,165                   | (3,434)                                    | 6,658                      | 164,038                       | 300,427           |
| <b>Changes in equity for 2016</b>  |                           |  |                            |                               |                   |
| Total comprehensive income   | -                         | -  | -                          | 109,567                       | 109,567           |
| Dividend distribution for 2015, Note 19 (d)  | -                         | -  | -                          | (132,846)                     | (132,846)         |
| Purchases of treasury shares, Note 19 (b)  | -                         | (1,140)                                    | -                          | -                             | (1,140)           |
| Share-based payments   | -                         | 2,087                                      | -                          | (2,087)                       | -                 |
| Sale of treasury shares, Note 22 (b)   | -                         | 857  | -                          | 123                           | 980               |
| Equity-settled transactions, Note 22 (b)   | -                         | -  | -                          | 1,262                         | 1,262             |
| Total contributions by and distributions to owners recognised directly in equity               | -                         | 1,804                                      | -                          | (133,548)                     | (131,744)         |
| <b>As at 31 December 2016</b>  | <b>133,165</b>            | <b>(1,630)</b>                             | <b>6,658</b>               | <b>140,057</b>                | <b>278,250</b>    |
| <b>As at 1 January 2017</b>  | 133,165                   | (1,630)                                    | 6,658                      | 140,057                       | 278,250           |
| <b>Changes in equity for 2017</b>  |                           |  |                            |                               |                   |
| Total comprehensive income   | -                         | -  | -                          | 64,283                        | 64,283            |
| Dividend distribution for 2016, Note 19 (d)  | -                         | -  | -                          | (119,735)                     | (119,735)         |
| Share-based payments   | -                         | 926  | -                          | (926)                         | -                 |
| Sale of treasury shares, Note 22 (b)   | -                         | 424  | -                          | (34)                          | 390               |
| Equity-settled transactions, Note 22 (b)   | -                         | -  | -                          | 268                           | 268               |
| Total contributions by and distributions to owners of the parent recognised directly in equity | -                         | 1,350                                      | -                          | (120,427)                     | (119,077)         |
| <b>As at 31 December 2017</b>  | <b>133,165</b>            | <b>(280)</b>                               | <b>6,658</b>               | <b>83,913</b>                 | <b>223,456</b>    |

Ericsson Nikola Tesla d.d.

# Statement of cash flows

for the year ended 31 December 2017

|  |           | 2017     | 2016     |
|--|-----------|----------|----------|
|  | Notes     | HRK '000 | HRK '000 |
| <b>Cash flows from operating activities</b>                                  |           |          |          |
| Profit before tax  |           | 68,507   | 117,668  |
| Adjustments for:   |           |          |          |
| Depreciation and amortisation  | 5, 10, 11 | 36,146   | 44,235   |
| Impairment losses and reversals  |           | 10,902   | 16,359   |
| Net increase in provisions   | 24        | 21,217   | 12,421   |
| Gain on sale of property, plant and equipment                                |           | (136)    | (65)     |
| Net loss/(gain) on remeasurement of financial assets                         |           | 644      | (2,033)  |
| Amortisation of discount   |           | 0        | (657)    |
| Interest income  |           | (4,936)  | (3,332)  |
| Interest expense   | 7         | 256      | 563      |
| Foreign exchange losses/(gains)  |           | 16,321   | (5,274)  |
| Equity-settled transactions  | 6         | 268      | 1,262    |
|  |           | 149,189  | 181,147  |
| Changes in working capital:  |           |          |          |
| In receivables   |           | (82,748) | (71,803) |
| In inventories   |           | (8,158)  | 10,571   |
| In payables  |           | 65,619   | 61,775   |
| Cash generated from operations   |           | 123,902  | 181,690  |
| Interest paid  |           | (256)    | (563)    |
| Income taxes paid  |           | (20,163) | -        |
| <b>Net cash from operating activities</b>                                    |           | 103,483  | 181,127  |
| <b>Cash flows from investing activities</b>                                  |           |          |          |
| Interest received  |           | 2,388    | 2,745    |
| Dividends received   |           | 77       | 212      |
| Investments in subsidiaries  | 13        | (1,019)  | -        |
| Proceeds from sale of property, plant and equipment                          |           | 149      | 83       |
| Purchases of property, plant and equipment, and intangible assets            |           | (26,450) | (28,224) |
| Deposits given to financial institutions - net                               |           | (2,200)  | (19,846) |
| Purchases of financial assets at fair value through profit and loss          |           | (54,008) | (89,000) |
| Proceeds from sale of financial assets at fair value through profit and loss |           | 31,760   | 81,745   |
| <b>Net cash used in investing activities</b>                                 |           | (49,303) | (52,285) |



Ericsson Nikola Tesla d.d.

# Statement of cash flows (continued)

for the year ended 31 December 2017

|   |        | 2017           | 2016           |
|---|--------|----------------|----------------|
|   | Notes  | HRK '000       | HRK '000       |
| <b>Cash flows from financing activities</b>                   |        |                |                |
| Purchase of treasury shares                                   | 19 (b) | -              | (1,140)        |
| Dividends paid  | 19 (d) | (119,887)      | (132,846)      |
| <b>Net cash used in financing activities</b>                  |        | (119,887)      | (133,986)      |
| Effects of exchange rate changes on cash and cash equivalents |        | (2,582)        | 20             |
| <b>Net decrease in cash and cash equivalents</b>              |        | (68,289)       | (5,124)        |
| Cash and cash equivalents at the beginning of the year        |        | 213,375        | 218,499        |
| <b>Cash and cash equivalents at the end of the year</b>       | 18     | <b>145,086</b> | <b>213,375</b> |

Notes to the Financial Statements of Ericsson Nikola Tesla d.d.

# 1 Significant accounting policies

## Reporting entity

Ericsson Nikola Tesla d.d. (the Company) is a joint stock company incorporated and domiciled in Croatia. The address of its registered office is Krapinska 45, 10000 Zagreb, the Republic of Croatia. The Company's shares are listed on the Public Joint Stock Company listing on the Zagreb Stock Exchange. A summary of the Company's principal accounting policies is set out below.

## Statement of compliance

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

## Basis of preparation

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

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

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

The Company has issued these separate financial statements in accordance with Croatian regulations. The Company has also prepared consolidated financial statements as at 31 December 2017 and for the year then ended in accordance with IFRS for the Company and its subsidiaries (the Group), which were approved by the Management Board on 25 April 2018. In the consolidated financial statements, subsidiary undertakings (listed in Note 13) and those companies in which the Group indirectly has an interest of more than half of the voting rights or otherwise has power to exercise control over the operations have been fully consolidated. Users of these non-consolidated financial statements should read them together with the Group's consolidated financial statements as at and for the year ended 31 December 2017 in order to obtain full information on the financial position, results of operations and changes in financial position of the Group as a whole.

## Going concern

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

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

# 1 Significant accounting policies (continued)

## Changes in accounting policies and disclosures

### (a) New and amended standards adopted by the Group

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

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

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

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

Certain new standards and interpretations have been published that are not mandatory for 31 December 2017 reporting periods and have not been early adopted by the Company. The Company's assessment of the impact of these new standards and interpretations is set out below:

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

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

The other financial assets held by the Company include:

- equity instruments currently classified as available for sale (AFS) for which a fair value through other comprehensive income (FVOCI) election is available
- equity investments currently measured at fair value through profit or loss (FVPL) which will continue to be measured on the same basis under IFRS 9, and
- debt instruments currently classified as held-to-maturity and measured at amortised cost which meet the conditions for classification at amortised cost under IFRS 9.

Accordingly, the Company does not expect the new guidance to affect the classification and measurement of these financial assets.

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

The new impairment model requires the recognition of impairment provisions based on expected credit losses (ECL) rather than only incurred credit losses as is the case under IAS 39. It applies to financial assets classified at amortised cost, debt instruments measured at FVOCI, contract assets under IFRS 15 Revenue from Contracts with Customers, lease receivables, loan commitments and certain financial guarantee contracts. Based on the assessments undertaken to date, the Company expects a small increase in the loss allowance for trade creditors and other financial assets by 0.5 to 1 million kuna.

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

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

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

# 1 Significant accounting policies (continued)

## Changes in accounting policies and disclosures (continued)

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

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

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

The new standard is based on the principle that revenue is recognised when control of a good or service transfers to a customer. The standard permits either a full retrospective or a modified retrospective approach for the adoption.

Management has assessed the effects of applying the new standard on the Company's financial statements and has identified the following areas that will be affected:

- Accounting for the extended warranty – If a supply contract includes explicit or implicit warranty terms that provide a customer with a service in addition (SIA) to the assurance that the HW/SW complies with agreed-upon specifications, the promised service is a separate performance obligation. The transaction price shall be allocated to the separately identified performance obligation of the promised service until the end of the contractual warranty period.
- Presentation of contract-related balances - The new requirement for classification and presentation of contract-related balances under IFRS 15 will result in a separate presentation of the contract asset and contract liability balances. At transition date, contract asset balance, estimated to be HRK 12.5 million, will be presented separately within current assets. Under previous standards these balances have been included within trade receivables as the accounting policy for 2017 states that trade receivables include amounts where risks and rewards have been transferred to the customer but not yet invoiced. Under IFRS 15, these balances will be presented as contract assets since the Company concluded that they relate to contract assets that are conditional on terms other than only the passage of time. At transition date, contract liability balance, estimated to be HRK 99 million, will be presented separately within current liabilities. Under previous standards these balances have been disclosed as deferred revenue within other current liabilities, and the Company concluded that they meet the definition of contract liability under IFRS 15.
- The Company has completed its assessment of the impact of IFRS 15 to its financial statements for all open contractual obligations per customer projects at transition date, 1 January 2018. Additional processes were implemented as part of the quantification exercise to accurately identify material transition impact, thus enabling it to be disclosed as part of the financial reporting process.

The impact of IFRS 15 implementation is estimated to be immaterial to equity at transition date.

This standard is mandatory for financial years commencing on or after 1 January 2018. The Company intends to adopt the standard using the modified retrospective approach which means that the cumulative impact of the adoption will be recognised in retained earnings as of 1 January 2018 and that comparatives will not be restated.

*IFRS 16 Leases (effective for annual periods beginning on or after 1 January 2019, early adoption is permitted only if IFRS 15 is adopted at the same time)*

IFRS 16 will affect primarily lessee accounting and will result in the recognition of almost all leases on the balance sheet. The standard removes the current distinction between operating and financing leases and requires recognition of an asset (the right to use the leased item) and a financial liability to pay rentals for virtually all lease contracts. An optional exemption exists for short-term and low-value leases.

The income statement will also be affected because the total expense is typically higher in the earlier years of a lease and lower in later years. Additionally, operating expense will be replaced with interest and depreciation, so key metrics like EBITDA will change.

Operating cash flows will be higher as cash payments for the principal portion of the lease liability are classified within financing activities. Only the part of the payments that reflects interest can continue to be presented as operating cash flows.

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

# 1 Significant accounting policies (continued)

## Changes in accounting policies and disclosures (continued)

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

Lessor accounting will not change significantly. Some differences may arise as a result of the new guidance on the definition of a lease. Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

The standard will affect primarily the accounting for the Company's operating leases. As at the reporting date, the Company has non-cancellable operating lease commitments of HRK 3,650 thousand, all due in 2018. At this stage, the Company is not able to estimate the total impact of the new standard on the Company's financial statements. It will make more detailed assessments of the impact over the next twelve months. The Management plans to adopt the standard on its effective date. The Company intends to apply the simplified transition approach and will not restate comparative amounts for the year prior to first adoption.

### Functional and presentational currency

The Company's financial statements have been prepared in Croatian kuna (HRK), which is the currency of the primary economic environment in which the entity operates (the functional currency) and the presentation currency, and are rounded to the nearest thousand. The closing exchange rate as at 31 December 2017 was HRK 6.26973 per USD 1 (2016: HRK 7.16854) and HRK 7.51365 per EUR 1 (2016: HRK 7.55779).

### Comparatives

As from 1 October 2017, the new segment structure as described in Note 4 on Segment reporting (Networks, Digital Services, Managed Services, Other) was introduced. Financial information for the previous period between 1 January and 31 December 2016, has been restated to the present segment structure. The restatement has no impact on the Statement of Comprehensive Income.

In order to ensure the comparability of data, the presentation of sales revenue in Note 3 for 2016 has been restated in accordance with the 2017 reporting method. To date, the principle of business unit analysis has been used, while the data in line with the new calculation has been obtained by analysing types of services. The reason for such new calculation method is frequent changes in units that do not provide the same data in the comparative period. As a result, an immaterial change in the amount of HRK 8.4 million occurred in 2016.

### Property, plant and equipment

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

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

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

# 1 Significant accounting policies (continued)

## Property, plant and equipment (continued)

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

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

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

## Intangible assets

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

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

## Impairment of assets

### a) Impairment of non-financial assets

Assets that have an indefinite useful life (such as 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.

### b) Impairment of financial assets

The Company assesses at each balance sheet date whether there is objective evidence that a financial asset or a group of financial assets is impaired. 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.

A provision for impairment of receivables is established when there is objective evidence that 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 original effective interest rate.

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

# 1 Significant accounting policies (continued)

## Financial instruments

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

### a) 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. The Company's loans and receivables comprise 'trade and other receivables', 'deposits' and 'cash and cash equivalents' in the balance sheet.

Loans and receivables are carried at amortised cost using the effective interest method.

### b) 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. Derivatives are also categorised as held for trading unless they are categorised as hedges. Assets in this category are classified as current assets if expected to be settled within 12 months; otherwise, they are classified as non-current.

Regular way purchases and sales of financial assets are recognised on trade-date – the date on which the Company commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. 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. Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active, the Company establishes fair value by using valuation techniques. These include the use of recent arm's length transactions and references to other instruments that are substantially the same, discounted cash flow analysis and option pricing models, making maximum use of market inputs and relying as little as possible on entity-specific inputs.

## Trade and other receivables

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

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

## Cash and cash equivalents

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

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

# 1 Significant accounting policies (continued)

## Trade and other payables

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

## Inventories

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

## Share capital

Share capital is stated in HRK at nominal value.

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

## Income tax

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

Deferred income tax is recognised by using the balance sheet liability method on temporary differences arising between tax basis of assets and liabilities and their carrying amount in the financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction does not affect either accounting or taxable profit or loss. Deferred tax assets and liabilities are not discounted and are classified as non-current assets and/or liabilities in the balance sheet. Deferred tax assets are recognised when it is probable that sufficient taxable profits will be available against which the deferred tax assets can be utilised. At each balance sheet date, the Company reassesses unrecognised deferred tax assets and the carrying amount of deferred tax assets.

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

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



Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

# 1 Significant accounting policies (continued)

## Foreign currencies

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

## Recognition of revenues

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

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

- **Delivery-type contracts:** Contracts for delivery of a product or a combination of products to form a whole or a part of a network as well as delivery of stand-alone products. Medium-size and large delivery type contracts generally include multiple elements. Such elements are normally standardized types of equipment or software as well as services such as network rollout.  
Revenue is recognized when risks and rewards have been transferred to the customer, normally stipulated in the contractual terms of trade. For delivery-type contracts that have multiple elements, revenue is allocated to each element based on relative fair values.
- **Construction-type contracts:** Contracts where the Company supplies to a customer a complete network, which to a large extent is based upon new technology or includes major components which are specifically designed for the customer. Revenues from construction-type contracts are recognized according to the stage of completion, using either the milestone output method or cost incurred method. Long-term construction contracts are assessed on a contract by contract basis and reflected in the statement of comprehensive income by recording revenue and related costs in line with the contract activity.
- **Service contracts:** Contracts for various services such as: training, consulting, engineering, installation, and multi-year managed services.  
Revenue is generally recognized when the services have been provided. Revenue for fixed price service contracts covering longer periods is recognized pro rata over the contract period.

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

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

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

# 1 Significant accounting policies (continued)

## Employee benefits

### a) Long-term service benefits

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

### b) Share-based payments

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

### c) Bonus plans

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

## Provisions

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

## Interest income

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

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

# 1 Significant accounting policies (continued)

## Segment reporting

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

## Borrowings

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

## Leases

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

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

## Dividend distribution

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

## Investments in subsidiaries

Investments in subsidiaries in which the Company has an interest of more than one half of the voting rights or otherwise has power to exercise control over the operations are recorded at cost less impairment losses, if any. Impairment is tested annually whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Investments in subsidiaries for which an impairment loss has been recorded are tested at each reporting date for a potential reversal of impairment.

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

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

# 1 Significant accounting policies (continued)

## Government grants

Grants from the government are recognised at their fair value where there is reasonable assurance that the grant will be received and the Company will comply with all attached conditions.

Government grants relating to costs are deferred and recognised in the statement of comprehensive income over the period necessary to match them with the costs that they are intended to compensate.

Government grants relating to property, plant and equipment are included in non-current liabilities as deferred government grants and are credited to the statement of comprehensive income on a straight-line basis over the expected lives of the related assets and presented within "other income".

# 2 Critical accounting estimates and judgements

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

## (a) Impairment losses on loans and receivables

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

## (b) Derecognition of receivables with off-balance sheet financing

In 2016, the Company entered into several new customer contracts in the foreign market. The contracts include delivery of equipment and sale of services with 15% up-front payment while remaining 85% have deferred payment terms up to 54 months.

The Company financed the sale of equipment through a Supplier credit arrangement. The arrangement includes:

i) matching cash receipts from customer with payments to the bank, ii) assignment of insurance policy to the bank, and iii) ceding future cash receipts from the customer to the bank through special purpose accounts secured by special purpose deposits (Note 12).

By transferring to the bank its contractual right to receive the cash flows, the Company transferred the financial asset to the bank. In terms of derecognition criteria, the Company analysed transfer of risk and rewards of the receivable, specifically related to credit risk and late payment risk.

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 2 Critical accounting estimates and judgements (continued)

### (b) Derecognition of receivables with off-balance sheet financing (continued)

The credit risk is shifted from international customer to the risk from domestic insurance company default which is considered as significant transfer in credit risk. The Company issued guarantees to the financing bank for risk of non-performance by the insurance company which is disclosed in Note 21. The issued guarantee for non-performance of the insurance company is recognized initially at fair value and subsequently at the higher of the unamortized balance of the initial fair value and the best estimate of expenditure required to settle the obligation under the guarantee.

Late payment risk was transferred based on the fact that the special purpose deposit covers the late payment charges and/or history of payments with the customer do not historically evidence late payment risk as substantial to the agreement.

Having transferred the right to cash flows and substantially all the risk and rewards relating to 90% of receivables, management concluded that it was appropriate to derecognize 90% of the related receivables from the balance sheet. The remaining 10% of the receivables remain on the balance sheet as long-term receivables from the customer (Note 12) and a 10% of the related financing liability to the bank is recorded as borrowings (Note 20).

Following derecognition, the residual difference between interest receivable from the customer and interest payable to the bank represents separate liability recognized at fair value and is disclosed in Note 20.

### c) Revenue recognition

The Company recognises revenues upon delivery of goods or service which may not always align with the timing of issuing invoices to customer since their timing is set in the contract. Revenues are recognised upon approved acceptance test by the customer. Consequently, the Company recognises deferred revenue (Note 25) and unbilled revenue (Note 15).

## 3 Sales revenue

|                             | 2017             | 2016             |
|-----------------------------|------------------|------------------|
|                             | HRK '000         | HRK '000         |
| Sales revenue from products | 441,729          | 404,498          |
| Sales revenue from services | 1,023,149        | 1,171,364        |
|                             | <u>1,464,878</u> | <u>1,575,862</u> |

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 4 Segment reporting

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

When determining the operating segments, the Group has looked at which market and to what type of customers the Group's products are aimed, and through what distribution channels they are sold, as well as to commonality regarding technology, research and development.

To best reflect the business focus and to facilitate comparability with the Ericsson Group, four operating segments are reported:

- Networks include radio and transport solutions with supporting services, based on industry standards and offered via scalable modular platforms. The portfolio enables customers to evolve their telecom networks across generations to 5G.
- Digital Services include products and services providing solutions for our Telecom and Industry & Society customers' digital transformation journeys across the support systems BSS and OSS, Telecom Core, and IT Cloud domains through a combination of products, technology and expertise in networks, software, cloud, and business processes.
- Managed Services are offered in three main areas: Networks, IT, and Network Design & Optimization.
- Other includes products and services that enable content owners, broadcasters, TV service providers and network operators to efficiently deliver, manage and monetize new TV experiences. In addition, segment Other includes iconectiv and emerging business such as Internet of Things and Unified Delivery Network (UDN).

The Management Board does not monitor assets and liabilities by segments and therefore this information is not disclosed. Revenues determined based on the geographic location of customers are disclosed in this note. All the Company's assets are located in Croatia.

|   | 2017      | 2016      |
|---|-----------|-----------|
|   | HRK '000  | HRK '000  |
| Sales revenue in domestic market  | 276,513   | 268,689   |
| Sales revenue in Belarus, Kazakhstan, Armenia, Moldova, Russia, Ukraine and Georgia | 125,461   | 283,801   |
| Sales revenue to Ericsson, Note 26 (a)  | 925,895   | 873,108   |
| Sales revenue in Bosnia and Herzegovina, Montenegro and Kosovo                      | 119,582   | 133,012   |
| Other export sales revenue  | 17,427    | 17,252    |
|   | 1,464,878 | 1,575,862 |

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 4 Segment reporting (continued)

|                     | Networks |          | Digital services |          | Managed services |          | Other    |          | Unallocated |          | Total     |           |
|---------------------|----------|----------|------------------|----------|------------------|----------|----------|----------|-------------|----------|-----------|-----------|
|                     | 2017     | 2016     | 2017             | 2016     | 2017             | 2016     | 2017     | 2016     | 2017        | 2016     | 2017      | 2016      |
|                     | HRK '000 | HRK '000 | HRK '000         | HRK '000 | HRK '000         | HRK '000 | HRK '000 | HRK '000 | HRK '000    | HRK '000 | HRK '000  | HRK '000  |
| Sales revenue       | 726,728  | 797,795  | 555,458          | 585,563  | 178,883          | 186,425  | 3,809    | 6,079    | -           | -        | 1,464,878 | 1,575,862 |
| Operating profit    | 93,385   | 72,456   | 19,613           | 59,660   | 2,566            | 4,708    | 589      | 1,253    | (44,931)    | (25,659) | 71,222    | 112,418   |
| Finance income      |          |          |                  |          |                  |          |          |          |             |          | (2,459)   | 5,813     |
| Finance expense     |          |          |                  |          |                  |          |          |          |             |          | (256)     | (563)     |
| Profit before tax   |          |          |                  |          |                  |          |          |          |             |          | 68,507    | 117,668   |
| Income tax          |          |          |                  |          |                  |          |          |          |             |          | (4,224)   | (8,101)   |
| Profit for the year |          |          |                  |          |                  |          |          |          |             |          | 64,283    | 109,567   |

## 5 Expenses by nature

|  | 2017             | 2016             |
|--|------------------|------------------|
|  | HRK '000         | HRK '000         |
| Changes in contract work in progress (Note 14)   | (8,164)          | 10,542           |
| Material and external services <sup>(1)</sup>  | 725,114          | 793,643          |
| Personnel expenses (Note 6)  | 654,105          | 609,405          |
| Depreciation and amortisation (Notes 10, 11)   | 36,146           | 44,235           |
| Less reclassifications in material and external services:<br>(Other income)/other operating expenses | (9,104)          | 7,249            |
|  | <u>1,398,097</u> | <u>1,465,074</u> |

<sup>(1)</sup> Including fees to auditors of HRK 520 thousand (2016: HRK 506 thousand). Fees to auditors mainly relate to statutory audit services. Other services provided by the firm providing statutory audit services include seminars and quality assurance related to impact of new accounting standards.

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 6 Personnel expenses

|   | 2017           | 2016           |
|---|----------------|----------------|
|   | HRK '000       | HRK '000       |
| Net salaries                              | 349,261        | 315,566        |
| Taxes and contributions                   | 270,925        | 264,303        |
| Other payroll-related costs               | 33,651         | 28,274         |
| Equity-settled transactions (Note 22 (b)) | 268            | 1,262          |
|   | <u>654,105</u> | <u>609,405</u> |

Personnel expenses include HRK 103,211 thousand (2016: HRK 95,049 thousand) of defined pension contributions paid or payable into obligatory pension plans. Contributions are calculated as a percentage of employees' gross salaries (Gross I).

Other payroll-related costs mainly relate to termination benefits in the amount of HRK 8,364 thousand (2016: HRK 4,091 thousand), and to transportation expenses and vacation accrual cost.

As at 31 December 2017, total number of employees was 2,268 (2016: 2,148).

## 7 Finance income and expense, net

|   | 2017         | 2016         |
|---|--------------|--------------|
|   | HRK '000     | HRK '000     |
| Interest income   | 2,733        | 3,332        |
| Net (loss)/gain from remeasurement of financial assets at fair value through profit or loss | (396)        | 2,283        |
| Amortization of discount  | (3)          | -            |
| Net foreign exchange (loss)/gain  | (4,793)      | 198          |
| Interest expense  | (256)        | (563)        |
|   | <u>2,715</u> | <u>5,250</u> |



Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 8 Income tax expense

Income tax has been calculated on the taxable income at statutory tax rate of 18% (2016: 20%). Income tax expense recognised in the consolidated statement of comprehensive income comprises:

|                            | 2017     | 2016     |
|----------------------------|----------|----------|
|                            | HRK '000 | HRK '000 |
| Current income tax expense | (5,002)  | (21,659) |
| Total deferred tax expense | 778      | 13,558   |
| Total income tax expense   | (4,224)  | (8,101)  |

### Effective tax rate reconciliation

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

|  | 2017     | 2016     |
|--|----------|----------|
|  | HRK '000 | HRK '000 |
| Profit before tax  | 68,507   | 117,668  |
| Income tax at 18% (2016: 20%)                                | 12,331   | 23,534   |
| Tax effects of:  |          |          |
| Expenses not deductible for tax purposes                     | 5,750    | 7,473    |
| Recognition of previously unrecognized temporary differences | (778)    | (13,558) |
| Tax incentives   | (13,079) | (829)    |
| Utilisation of tax losses                                    | -        | (8,519)  |
| Tax charge   | 4,224    | 8,101    |
| Effective tax rate   | 6.2%     | 6.9%     |

Tax incentives totalling HRK 13,079 thousand (2016: HRK 829 thousand) include tax allowances for certain expenditure, as employment and education and training, as defined by Croatian tax legislation. The underlying expenditure is included in cost of sales.

The Croatian Income Tax Act is subject to different interpretations and changes in respect of certain expenses which reduce the tax base. The Management Board's interpretation of the law relating to these transactions and activities of the Company may be disputed by the relevant authorities. The Tax Authority may take a different view in interpreting the laws and judgments, and it is possible that those transactions and activities that have not been disputed in the past may be disputed now. The Tax Authority may carry out a tax audit within three years from the year in which the income tax liability for a certain financial period was established.

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 8 Income tax expense (continued)

### Deferred tax from other temporary differences

During 2016, the Company re-evaluated the potential for utilization of certain existing temporary differences for which deferred tax assets had not been previously recognized based on the uncertainty of their utilization. In view of the changed circumstances, the Company recognized deferred tax assets in the amount of HRK 14,336 thousand (2016: HRK 13,558 thousand) relating to temporary differences arising from:

- Accrued interest expenses;
- Impairment of receivables;
- Accrued expenses from contracts;
- Warranty provisions and
- Provisions for jubilee awards and retirement.

|                                      | Impairments, provisions and accrued expenses<br>HRK '000 |
|--------------------------------------|--|
| As at 1 January 2016                 | -  |
| Tax credited to the Income statement | 13,558   |
| Tax charged to the Income statement  | -  |
| As at 31 December 2016               | <u>13,558</u>  |
| As at 1 January 2017                 | 13,558   |
| Tax credited to the Income statement | 7,894  |
| Tax charged to the Income statement  | <u>(7,116)</u>   |
| As at 31 December 2017               | <u>14,336</u>  |

## 9 Earnings per share

|   | 2017             | 2016             |
|---|------------------|------------------|
| Profit for the year (HRK '000)                                | 64,283           | 109,567          |
| Weighted Average Number of Shares Outstanding at the year-end | <u>1,330,499</u> | <u>1,328,809</u> |
| Earnings per share (HRK)                                      | <u>48.32</u>     | <u>82.45</u>     |

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

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

# 10 Property, plant and equipment

|                                    | Land and<br>buildings<br>HRK '000 | Plant and<br>equipment<br>HRK '000 | Other<br>HRK '000 | Total<br>HRK '000 |
|------------------------------------|-----------------------------------|------------------------------------|-------------------|-------------------|
| <b>As at 1 January 2016</b>        |                                   |                                    |                   |                   |
| Cost or valuation                  | 160,367                           | 363,505                            | 328               | 524,200           |
| Accumulated depreciation           | (115,966)                         | (281,715)                          | (237)             | (397,918)         |
| Net book amount                    | 44,401                            | 81,790                             | 91                | 126,282           |
| <b>Year ended 31 December 2016</b> |                                   |                                    |                   |                   |
| Opening net book amount            | 44,401                            | 81,790                             | 91                | 126,282           |
| Additions                          | 1,797                             | 23,644                             | -                 | 25,441            |
| Disposals                          | -                                 | (2)                                | -                 | (2)               |
| Depreciation charge                | (2,955)                           | (40,825)                           | (8)               | (43,788)          |
| Closing net book amount            | 43,243                            | 64,607                             | 83                | 107,933           |
| <b>As at 31 December 2016</b>      |                                   |                                    |                   |                   |
| Cost or valuation                  | 162,164                           | 366,900                            | 328               | 529,392           |
| Accumulated depreciation           | (118,921)                         | (302,293)                          | (245)             | (421,459)         |
| Net book amount                    | 43,243                            | 64,607                             | 83                | 107,933           |
| <b>Year ended 31 December 2017</b> |                                   |                                    |                   |                   |
| Opening net book amount            | 43,243                            | 64,607                             | 83                | 107,933           |
| Additions                          | 5,500                             | 20,117                             | -                 | 25,617            |
| Disposals                          | -                                 | (17)                               | -                 | (17)              |
| Depreciation charge                | (3,066)                           | (32,448)                           | (8)               | (35,522)          |
| Closing net book amount            | 45,677                            | 52,259                             | 75                | 98,011            |
| <b>As at 31 December 2017</b>      |                                   |                                    |                   |                   |
| Cost or valuation                  | 167,664                           | 365,692                            | 328               | 533,684           |
| Accumulated depreciation           | (121,987)                         | (313,433)                          | (253)             | (435,673)         |
| Net book amount                    | 45,677                            | 52,259                             | 75                | 98,011            |

As at 31 December 2017, the Company had contracts totalling HRK 4,293 thousand (2016: HRK 2,567 thousand) related to future equipment purchases.

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 10 Property, plant and equipment (continued)

The Company acts as a lessor under operating leases, mainly in respect of land and buildings. Property leased to others with a carrying value of HRK 11,281 thousand (2016: HRK 12,786 thousand) is included within land and buildings. These assets are depreciated at the same depreciation rates as other buildings. Subsequent renewals are negotiated with the lessee. No contingent rents are charged. Portions of the property which is held for rental could not be sold separately or leased out separately under finance lease. Consequently, the IAS 40 criteria for separate investment property recognition are not met.

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

|                            | 2017     | 2016     |
|----------------------------|----------|----------|
|                            | HRK '000 | HRK '000 |
| Less than one year         | 3,285    | 3,271    |
| Between one and five years | 1,643    | 1,635    |
|                            | 4,928    | 4,906    |

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

# 11 Intangible assets

The movement on intangible assets in the year ended 31 December 2017 may be analysed as follows:

|                                    | Application<br>software<br>HRK '000 |
|------------------------------------|-------------------------------------|
| <b>As at 1 January 2016</b>        |                                     |
| Cost or valuation                  | 8,470                               |
| Accumulated amortization           | (7,656)                             |
| Net book amount                    | <u>814</u>                          |
| <b>Year ended 31 December 2016</b> |                                     |
| Opening net book amount            | 814                                 |
| Additions                          | 1,545                               |
| Amortization charge                | (447)                               |
| Closing net book amount            | <u>1,912</u>                        |
| <b>As at 31 December 2016</b>      |                                     |
| Cost or valuation                  | 10,014                              |
| Accumulated amortization           | (8,102)                             |
| Net book amount                    | <u>1,912</u>                        |
| <b>Year ended 31 December 2017</b> |                                     |
| Opening net book amount            | 1,912                               |
| Additions                          | -                                   |
| Disposals                          | (1)                                 |
| Amortization charge                | (624)                               |
| Closing net book amount            | <u>1,287</u>                        |
| <b>As at 31 December 2017</b>      |                                     |
| Cost or valuation                  | 5,726                               |
| Accumulated amortization           | (4,439)                             |
| Net book amount                    | <u>1,287</u>                        |

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 12 Loans and receivables

|   | 2017          | 2016          |
|---|---------------|---------------|
|   | HRK '000      | HRK '000      |
| Deposits with financial institutions, denominated in foreign currency           | 15,495        | 28,117        |
| Deposits with financial institutions, denominated in HRK                        | 12,360        | -             |
| Non-current receivables from foreign customers, denominated in foreign currency | 46,413        | 42,889        |
| Loans given, Note 2 (b)   | 11,498        | 10,119        |
| Non-current receivables from domestic customers, denominated in HRK             | 1,552         | 2,922         |
| Receivables for sold apartments   | 544           | 606           |
| Total loans and receivables   | 87,862        | 84,653        |
| Impairment allowance on loans and receivables                                   | (4,988)       | (3,493)       |
|   | <u>82,874</u> | <u>81,160</u> |

Deposits with financial institutions in the amount of HRK 23,721 thousand (2016: 23,959 thousand) are used as a collateral for Supplier credit arrangement disclosed in Note 2 (b), with interest rate from 0.75% to 2% and maturing in year 2022.

The remainder of the deposits with financial institutions in the amount of HRK 4,134 thousand (2016: HRK 4,159 thousand) are placed as guarantee deposits for housing loans provided to the employees, at 25% 12M EUR LIBOR rate, and with a remaining maturity of over three years.

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

### Non-current portion of foreign and domestic loans and receivables from customers

|      | 2017          | 2016          |
|------|---------------|---------------|
| Due  | HRK '000      | HRK '000      |
| 2018 | -             | 33,661        |
| 2019 | 39,388        | 9,214         |
| 2020 | 10,983        | 8,017         |
| 2021 | 8,548         | 5,038         |
| 2022 | 544           | -             |
|      | <u>59,463</u> | <u>55,930</u> |

Housing loans to employees are linked to the counter value of euro, repayments are made by deduction from monthly salary and the loans are secured with collateral on the house or apartment. Receivables for sold apartments and housing loans provided to a limited number of employees bear fixed interest rates of up to 5% per annum.

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 13 Investments in subsidiaries

|  |           | 2017     | 2016     |
|--|-----------|----------|----------|
|  | Ownership | HRK '000 | HRK '000 |
| Ericsson Nikola Tesla BY d.o.o.                      | 100%      | 1,020    | -        |
| Ericsson Tesla SoftLab d.o.o.                        | 100%      | 20       | 20       |
| ETK poslovna rješenja d.o.o.                         | 100%      | 20       | 20       |
| Ericsson Nikola Tesla Servisi d.o.o.                 | 100%      | 20       | 20       |
| Libratel d.o.o                                       | 100%      | 5        | 5        |
| Ericsson Nikola Tesla BH d.o.o                       | 100%      | 7        | 7        |
| Ericsson Nikola Tesla d.d. – Branch office of Kosovo | 100%      | 1        | 1        |
|  |           | 1,093    | 73       |

The subsidiaries Ericsson Tesla SoftLab d.o.o. and ETK poslovna rješenja d.o.o. are inactive, while others listed above are active and fully consolidated in the consolidated financial statements.

The new subsidiary Ericsson Nikola Tesla BY d.o.o. was founded in 2017 in Belarus. The subsidiary provides local customer support services.

## 14 Inventories

|                           | 2017     | 2016     |
|---------------------------|----------|----------|
|                           | HRK '000 | HRK '000 |
| Raw materials             | 82       | 463      |
| Contract work in progress | 17,348   | 9,184    |
| Total inventories         | 17,430   | 9,647    |
| Impairment allowance      | (82)     | (459)    |
|                           | 17,348   | 9,188    |

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

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 15 Trade receivables

|   | 2017           | 2016           |
|---|----------------|----------------|
|   | HRK '000       | HRK '000       |
| Foreign trade receivables                           | 77,450         | 102,848        |
| Current portion of non-current foreign receivables  | 14,994         | 18,452         |
| Total current foreign receivables                   | 92,444         | 121,300        |
| Domestic trade receivables                          | 55,474         | 62,498         |
| Current portion of non-current domestic receivables | 67             | -              |
| Total current domestic receivables                  | 55,541         | 62,498         |
| Impairment allowance on receivables                 | (7,183)        | (10,435)       |
|   | <u>140,802</u> | <u>173,363</u> |

Included in trade receivables is HRK 4,050 thousand (2016: HRK 7,799 thousand) of unbilled revenue.

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

|  | 2017          | 2016          |
|--|---------------|---------------|
|  | HRK '000      | HRK '000      |
| As at 1 January  | 15,513        | 7,477         |
| Provision for receivables impaired during the year       | 12,715        | 21,571        |
| Impact of discounting non-current receivables            | 1,956         | 3,135         |
| Receivables written off during the year as uncollectible | (13,369)      | (11,112)      |
| Unused amounts reversed                                  | (3,233)       | (4,901)       |
| Amortisation of discount                                 | -             | (657)         |
| As at 31 December <sup>(1)</sup>                         | <u>13,582</u> | <u>15,513</u> |

<sup>1)</sup> Including impairment provision for receivables from related parties of HRK 1,411 thousand (2016: HRK 1,585 thousand)



Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 16 Other receivables

|                             | 2017          | 2016          |
|-----------------------------|---------------|---------------|
|                             | HRK '000      | HRK '000      |
| Receivables from employees  | 405           | 938           |
| Accrued interest receivable | 529           | 99            |
| Advances given              | 14,129        | 11,722        |
| Other receivables           | 2,512         | 1,281         |
|                             | <u>17,575</u> | <u>14,040</u> |

## 17 Financial assets at fair value through profit or loss

|   | 2017          | 2016          |
|---|---------------|---------------|
|   | HRK '000      | HRK '000      |
| Financial assets at fair value through profit or loss |               |               |
| - Equity securities                                   | 1,387         | 1,952         |
| - Investment in open-ended investment funds           | 83,133        | 61,041        |
|   | <u>84,520</u> | <u>62,993</u> |

## 18 Cash and cash equivalents

|                          | 2017           | 2016           |
|--------------------------|----------------|----------------|
|                          | HRK '000       | HRK '000       |
| Cash and demand deposits | 145,086        | 213,375        |
|                          | <u>145,086</u> | <u>213,375</u> |

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 19 Equity

### (a) Share capital

As at 31 December 2017, the share capital of the Company is represented by 1,331,650 (2016: 1,331,650) of authorised, issued and fully paid ordinary shares, with a total registered value of HRK 133,165 thousand (2016: HRK 133,165 thousand). The nominal value of one share is HRK 100 (2016: HRK 100). The holders of the ordinary shares are entitled to receive dividends as declared at the General Assembly and are entitled to one vote per share at the General Assembly.

The Company's shareholders as at 31 December are:

|                                 | Number of shares | % held        | Number of shares | % held        |
|---------------------------------|------------------|---------------|------------------|---------------|
|                                 | 2017             |               | 2016             |               |
| Telefonaktiebolaget LM Ericsson | 653,473          | 49.07         | 653,473          | 49.07         |
| Small shareholders              | 677,931          | 50.91         | 676,682          | 50.81         |
| Treasury shares                 | 246              | 0.02          | 1,495            | 0.12          |
|                                 | <u>1,331,650</u> | <u>100.00</u> | <u>1,331,650</u> | <u>100.00</u> |

### (b) Treasury shares

These shares are held initially as "treasury shares" and are regularly granted to key management and other employees as a part of the share-based program established during 2004, as described in Note 22 (b). During 2017, the Company did not purchase its own shares.

Movements in treasury shares are as follows:

|                                 | Number of shares | Number of shares |
|---------------------------------|------------------|------------------|
|                                 | 2017             | 2016             |
| As at 1 January (Note 19 (a))   | 1,495            | 3,382            |
| Purchased during the year       | -                | 1,000            |
| Distributed during the year     | (1,249)          | (2,887)          |
| As at 31 December (Note 19 (a)) | <u>246</u>       | <u>1,495</u>     |

### (c) Legal reserves

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

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 19 Equity (continued)

### (d) Proposed dividends

Dividends payable are not accounted for until they have been ratified at the General Assembly of shareholders. On 6 June 2017, the General Assembly approved a regular dividend in respect of 2016 of HRK 20.00 per share, and an additional extraordinary dividend of HRK 70.00 per share, totalling HRK 119,735 thousand.

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

|                               | 2017           | 2016           |
|-------------------------------|----------------|----------------|
|                               | HRK '000       | HRK '000       |
| HRK 90.00 per share for 2016  | 119,735        | -              |
| HRK 100.00 per share for 2015 | -              | 132,846        |
| Prior year dividend payout    | 152            | -              |
|                               | <u>119,887</u> | <u>132,846</u> |

## 20 Borrowings

|   | 2017         | 2016         |
|---|--------------|--------------|
|   | HRK '000     | HRK '000     |
| Borrowings, Note 2 (b)                            | <u>8,378</u> | <u>8,954</u> |
| Changes in liabilities from financing activities: |              |              |
| Year ended 31 December 2016                       |              | HRK '000     |
| Opening net book amount                           |              | -            |
| Other non-cash movements                          |              | <u>8,954</u> |
| Closing net book amount                           |              | <u>8,954</u> |
| Year ended 31 December 2017                       |              |              |
| Opening net book amount                           |              | 8,954        |
| Foreign exchange differences                      |              | <u>(576)</u> |
| Closing net book amount                           |              | <u>8,378</u> |

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 21 Other non-current liabilities

|  | 2017         | 2016         |
|--|--------------|--------------|
|  | HRK '000     | HRK '000     |
| Accounts payable                             | 1,546        | 2,400        |
| NPV discount                                 | (392)        | (358)        |
| Total accounts payable /i/                   | 1,154        | 2,042        |
| Liabilities for issued guarantee, Note 2 (b) | 648          | 782          |
| Other non-current liabilities, Note 2 (b)    | 5,041        | 7,122        |
|  | <u>6,843</u> | <u>9,946</u> |

/i/ The non-current payable to Ericsson Nikola Tesla Servisi d.o.o. (EHR) relates to the five-year managed services contract with Hrvatski Telekom.

## 22 Employee benefits

### (a) Long-term service benefits

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

However, the Company pays a one-time benefit amounting to HRK 8,000 for each employee who retires. Additionally, the Company pays jubilee awards in respect of each 5 years of service, of an employee, starting from the 10th year and ending in the 40th year. The principal actuarial assumptions used to determine retirement and jubilee obligations as at 31 December 2017 were a 6% discount rate (2016: 6%) and a 7.12% (2016: 4.17%) rate of average employment turnover.

Movements in long-term service benefits were as follows:

|                                      | Jubilee<br>awards | Retirement | Total        | Jubilee<br>awards | Retirement   | Total        |
|--------------------------------------|-------------------|------------|--------------|-------------------|--------------|--------------|
|                                      | 2017              |            |              | 2016              |              |              |
|                                      | HRK '000          | HRK '000   | HRK '000     | HRK '000          | HRK '000     | HRK '000     |
| As at 1 January                      | 4,455             | 1,032      | 5,487        | 4,584             | 1,039        | 5,623        |
| Obligation created during the year   | 555               | 253        | 808          | 649               | 324          | 973          |
| Obligation fulfilled during the year | (453)             | (8)        | (461)        | (634)             | (16)         | (650)        |
| Obligation reversed during the year  | (20)              | (535)      | (555)        | (144)             | (315)        | (459)        |
| As at 31 December                    | <u>4,537</u>      | <u>742</u> | <u>5,279</u> | <u>4,455</u>      | <u>1,032</u> | <u>5,487</u> |

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 22 Employee benefits (continued)

### (a) Long-term service benefits (continued)

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

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

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

### (b) Share-based payments

Part of the share-based programme from 2014 relates to the right of employee to purchase certain shares, which are settled according to fair value relevant at the date of the purchase. Based on this programme, the Company sold to its employees 372 shares (2016: 841 shares) and received compensation in the amount of HRK 390 thousand (2016: HRK 980 thousand). The difference between the purchase price of the shares and selling price received from the employee in the amount of HRK 34 thousand (2016: HRK 123 thousand) has been recognised within retained earnings.

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

|                   | 2017             | 2016             |
|-------------------|------------------|------------------|
|                   | Number of shares | Number of shares |
| As at 1 January   | 1,297            | 4,557            |
| Granted           | 2                | -                |
| Exercised         | (1,249)          | (2,887)          |
| Expired           | (25)             | (373)            |
| As at 31 December | 25               | 1,297            |

Vesting conditions for shares granted under Loyalty program are two to five years of service.

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

|   | Number<br>of granted<br>shares | Weighted average fair value<br>per share at grant date<br>HRK |
|---|--------------------------------|---|
| Reversal in 2015 of shares granted in 2011-2013 | 373                            | 1,373.20  |
| Reversal in 2016 of shares granted in 2011-2013 | 25                             | 1,373.20  |

During 2017, the Company recognised HRK 268 thousand (2016: HRK 1,262 thousand) of expenses in respect of share-based payments, which are included in personnel expenses as disclosed in Note 6.

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 23 Trade and other payables

|                           | 2017           | 2016           |
|---------------------------|----------------|----------------|
|                           | HRK '000       | HRK '000       |
| Trade payables            | 86,802         | 26,628         |
| Liabilities to employees  | 91,901         | 82,422         |
| Other current liabilities | 16,654         | 15,350         |
| Net liability for VAT     | 1,766          | 6,060          |
|                           | <u>197,123</u> | <u>130,460</u> |

## 24 Provisions

Movements in provisions were as follows:

|                                 | Warranty<br>reserve | Penalty<br>reserve | Termination<br>benefits | Other<br>provisions | Total           |
|---------------------------------|---------------------|--------------------|-------------------------|---------------------|-----------------|
|                                 | HRK '000            | HRK '000           | HRK '000                | HRK '000            | HRK '000        |
| As at 1 January 2016            | <u>5,350</u>        | <u>1,785</u>       | <u>2,648</u>            | -                   | <u>9,783</u>    |
| Additional provisions           | 8,524               | -                  | 3,937                   | 497                 | 12,958          |
| Unused provisions reversed      | (129)               | (408)              | -                       | -                   | (537)           |
| Provisions used during the year | <u>(2,245)</u>      | <u>(902)</u>       | <u>(3,090)</u>          | -                   | <u>(6,237)</u>  |
| As at 31 December 2016          | <u>11,500</u>       | <u>475</u>         | <u>3,495</u>            | <u>497</u>          | <u>15,967</u>   |
| As at 1 January 2017            | <u>11,500</u>       | <u>475</u>         | <u>3,495</u>            | <u>497</u>          | <u>15,967</u>   |
| Additional provisions           | 8                   | -                  | 6,251                   | 15,504              | 21,763          |
| Unused provisions reversed      | (71)                | (475)              | -                       | -                   | (546)           |
| Provisions used during the year | <u>(2,662)</u>      | -                  | <u>(7,406)</u>          | <u>(497)</u>        | <u>(10,565)</u> |
| As at 31 December 2017          | <u>8,775</u>        | -                  | <u>2,340</u>            | <u>15,504</u>       | <u>26,619</u>   |

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

Followed by the prudence principle and based on the circumstances and other factors, including expectations of future events, provision in the amount of HRK 15,504 thousand was made to a complex project in the Community of Independent States market.

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 25 Accrued charges and deferred revenue

|   | 2017     | 2016     |
|---|----------|----------|
|   | HRK '000 | HRK '000 |
| Advances from domestic customers                | 1,122    | 96       |
| Advances from foreign customers                 | 3,107    | 19,755   |
| Deferred revenue                                | 103,645  | 104,905  |
| Accrued charges for unused holidays             | 18,323   | 17,978   |
| Accrued charges in respect of service contracts | 33,461   | 34,109   |
| Other accrued charges                           | 31,653   | 28,382   |
|   | 191,311  | 205,225  |

Deferred revenue represents amounts due to customers under contracts for work not performed but invoices issued or cash received and thus present a liability to perform a service or delivery.

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

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 26 Balances and transactions with related parties

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

The Company is a related party to the Ericsson Group via the 49.07% (2016: 49.07%) shareholding by Telefonaktiebolaget LM Ericsson, which is also the ultimate parent of the Ericsson Group.

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

### (a) Key transactions with the related parties

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

|                                 | Telefonaktiebolaget<br>LM Ericsson |          | Other Ericsson Group<br>consolidated companies |          | Subsidiaries |          | Total    |          |
|---------------------------------|------------------------------------|----------|--|----------|--------------|----------|----------|----------|
|                                 | 2017                               | 2016     | 2017   | 2016     | 2017         | 2016     | 2017     | 2016     |
|                                 | HRK '000                           | HRK '000 | HRK '000                                       | HRK '000 | HRK '000     | HRK '000 | HRK '000 | HRK '000 |
| Sales of goods and services     |                                    |          |  |          |              |          |          |          |
| Sales revenue                   | -                                  | -        | 925,895  | 873,108  | 1,593        | 2,077    | 927,488  | 875,185  |
| Other income                    | -                                  | -        | 10,198   | 38,406   | 147          | 215      | 10,345   | 38,621   |
|                                 | -                                  | -        | 936,093  | 911,514  | 1,740        | 2,292    | 937,833  | 913,806  |
| Purchases of goods and services |                                    |          |  |          |              |          |          |          |
| Licences                        | 2,645                              | 3,448    | 18,853   | 20,890   | -            | -        | 21,498   | 24,338   |
| Cost of sales                   | -                                  | -        | 217,790  | 369,671  | 178,681      | 190,520  | 396,471  | 560,191  |
| Other expenses                  | -                                  | -        | -  | -        | (309)        | -        | (309)    | -        |
|                                 | 2,645                              | 3,448    | 236,643  | 390,561  | 178,372      | 190,520  | 417,660  | 584,529  |

The sales of goods and services transactions have been directly negotiated between the involved parties and agreed on an individual basis. The Company pays: (i) licence fees on sales of services and wireline products, (ii) corporate trade mark licences, (iii) support services, (iv) R&D tools and (v) IS/IT fee. The licence fee is paid as a percentage of sales of services and sales of wireline products.



Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 26 Balances and transactions with related parties (continued)

### (b) Key management compensation

The Company's key management include the executive management listed on page 172, comprising the Management Board member and directors of the main organisational units.

|   | 2017          | 2016          |
|---|---------------|---------------|
|   | HRK '000      | HRK '000      |
| Salaries and other short-term employee benefits | 22,063        | 22,619        |
| Other long-term benefits                        | 17            | 17            |
|   | <u>22,080</u> | <u>22,636</u> |

The members of the executive management and the Supervisory Board held 5,076 ordinary shares at the year-end (2016: 4,627 shares).

In addition, the Company paid remuneration totalling HRK 346 thousand (2016: HRK 357 thousand) to the Supervisory Board and Audit Committee members during 2017.

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

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

|   | Trade receivable |               | Trade payable  |               |
|---|------------------|---------------|----------------|---------------|
|   | 2017             | 2016          | 2017           | 2016          |
|   | HRK '000         | HRK '000      | HRK '000       | HRK '000      |
| Telefonaktiebolaget LM Ericsson (LME), main shareholder | 10               | -             | 57             | 1,650         |
| Other Ericsson Group companies                          | 104,474          | 88,857        | 112,693        | 66,716        |
| Subsidiaries:   |                  |               |                |               |
| Ericsson Nikola Tesla BH d.o.o.                         | 144              | 64            | 595            | 353           |
| Ericsson Nikola Tesla Servişi d.o.o.                    | 82,069           | 920           | 21,924         | 27,357        |
| Ericsson Nikola Tesla d.d. – Branch office of Kosovo    | 160              | 293           | -              | -             |
| Libratel d.o.o.   | -                | 7             | -              | 135           |
| Ericsson Nikola Tesla BY                                | -                | -             | 239            | -             |
|   | <u>186,857</u>   | <u>90,141</u> | <u>135,508</u> | <u>96,211</u> |

The Company recorded a non-current receivable (Note 12) and deferred revenue (within other non-current liabilities) of HRK 1,156 thousand (2016: HRK 2,042 thousand) from Ericsson Services d.o.o. (ESK) relating to the five-year managed services contract with Hrvatski Telekom.

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 27 Financial risk management

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

### (a) Currency risk

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

As at 31 December 2017, if the euro and US dollar had weakened/strengthened by 1% (2016: +/-1%) against the Croatian kuna, with all other variables held constant, the net result after tax for the reporting period would have been HRK 2,364 thousand higher/lower for the Company (2016: HRK 2,913 thousand), mainly as a result of foreign exchange losses/gains on translation of cash, cash equivalents, deposits, trade payables, customer receivables and customer financing denominated in euro.

The Company continues to focus on securing natural hedges and active currency management and to minimise impacts from currency moves. The Company's exposure to foreign currencies is shown in the table below.

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 27 Financial risk management (continued)

### (a) Currency risk (continued)

The tables below present the currency analysis and resulting gap.

| 2017  | EUR            | USD            | Other<br>currency | Total<br>foreign<br>currencies | HRK            | Total          |
|---|----------------|----------------|-------------------|--------------------------------|----------------|----------------|
|   | HRK '000       | HRK '000       | HRK '000          | HRK '000                       | HRK '000       | HRK '000       |
| Loans and receivables                                 | 4,134          | 68,918         | -                 | 73,052                         | 9,822          | 82,874         |
| Trade and other receivables                           | 117,807        | 57,251         | 2,060             | 177,118                        | 168,116        | 345,234        |
| Financial assets at fair value through profit or loss | -              | -              | -                 | -                              | 84,520         | 84,520         |
| Cash and cash equivalents                             | 73,220         | 10,371         | 6,233             | 89,824                         | 55,262         | 145,086        |
|   | <u>195,161</u> | <u>136,540</u> | <u>8,293</u>      | <u>339,994</u>                 | <u>317,720</u> | <u>657,714</u> |
| Borrowings  | -              | 8,378          | -                 | 8,378                          | -              | 8,378          |
| Trade and other payables                              | 32,875         | 14,989         | 469               | 48,333                         | 291,481        | 339,814        |
|   | <u>32,875</u>  | <u>23,367</u>  | <u>469</u>        | <u>56,711</u>                  | <u>291,481</u> | <u>348,192</u> |
| Currency gap  | <u>162,286</u> | <u>113,173</u> | <u>7,824</u>      | <u>283,283</u>                 | <u>26,239</u>  | <u>309,522</u> |

| 2016  | EUR            | USD            | Other<br>currency | Total<br>foreign<br>currencies | HRK            | Total          |
|---|----------------|----------------|-------------------|--------------------------------|----------------|----------------|
|   | HRK '000       | HRK '000       | HRK '000          | HRK '000                       | HRK '000       | HRK '000       |
| Loans and receivables                                 | 4,159          | 73,831         | -                 | 77,990                         | 3,170          | 81,160         |
| Trade and other receivables                           | 117,436        | 72,936         | 1,876             | 192,248                        | 85,296         | 277,544        |
| Financial assets at fair value through profit or loss | -              | -              | -                 | -                              | 62,993         | 62,993         |
| Cash and cash equivalents                             | 115,175        | 37,844         | 166               | 153,185                        | 60,190         | 213,375        |
|   | <u>236,770</u> | <u>184,611</u> | <u>2,042</u>      | <u>423,423</u>                 | <u>211,649</u> | <u>635,072</u> |
| Borrowings  | -              | 8,954          | -                 | 8,954                          | -              | 8,954          |
| Trade and other payables                              | 56,666         | 18,700         | 284               | 75,650                         | 182,625        | 258,275        |
|   | <u>56,666</u>  | <u>27,654</u>  | <u>284</u>        | <u>84,604</u>                  | <u>182,625</u> | <u>267,229</u> |
| Currency gap  | <u>180,104</u> | <u>156,957</u> | <u>1,758</u>      | <u>338,819</u>                 | <u>29,024</u>  | <u>367,843</u> |

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 27 Financial risk management (continued)

### (b) Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. As the Company mainly has its customer financing at a fixed interest rate and only a small portion of customer financing is affected by possible changes in market interest rates, the risk of fluctuating market interest rates is considered low. The Company also has deposits in financial institutions at a variable interest rate.

As at 31 December 2017:

- if the effective EUR interest rate on EUR deposits had increased/decreased by 1% (2016: 1%) on an annual level, the net result due to changes in EUR deposits after tax for the reporting period would have been HRK 34 thousand higher/lower (2016: HRK 33 thousand);
- if the effective HRK interest rate on HRK deposits had increased/decreased by 1% (2016: 1%) on an annual level, the net result due to changes in investment funds after tax for the reporting period would have been HRK nil thousand higher/lower (2016: HRK 488 thousand).

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

|   | Average interest rates | Average interest rates |
|---|------------------------|------------------------|
|   | 2017                   | 2016                   |
|   | %                      | %                      |
| Loans and receivables                                 | 2.73                   | 2.59                   |
| Trade and other receivables                           | -                      | -                      |
| Financial assets at fair value through profit or loss | -                      | -                      |
| Cash and cash equivalents                             | 0.11                   | 0.21                   |

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 27 Financial risk management (continued)

### (b) Interest rate risk (continued)

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

| 2017  | Non-interest-bearing | Up to 1 month  | 1 - 3 months | 3 - 12 months | 1 - 5 years | Over 5 years | Total          | Fixed interest |
|---|----------------------|----------------|--------------|---------------|-------------|--------------|----------------|----------------|
|   | HRK '000             | HRK '000       | HRK '000     | HRK '000      | HRK '000    | HRK '000     | HRK '000       | HRK '000       |
| Loans and receivables                                 | 53,831               | -              | 774          | 414           | -           | 4,134        | 59,153         | 23,721         |
| Trade and other receivables                           | 345,234              | -              | -            | -             | -           | -            | 345,234        | -              |
| Financial assets at fair value through profit or loss | 84,520               | -              | -            | -             | -           | -            | 84,520         | -              |
| Cash and cash equivalents                             | -                    | 145,086        | -            | -             | -           | -            | 145,086        | -              |
|   | <u>483,585</u>       | <u>145,086</u> | <u>774</u>   | <u>414</u>    | <u>-</u>    | <u>4,134</u> | <u>633,993</u> | <u>23,721</u>  |
| Borrowings  | 8,378                | -              | -            | -             | -           | -            | 8,378          | -              |
| Trade and other payables                              | 339,814              | -              | -            | -             | -           | -            | 339,814        | -              |
|   | <u>348,192</u>       | <u>-</u>       | <u>-</u>     | <u>-</u>      | <u>-</u>    | <u>-</u>     | <u>348,192</u> | <u>-</u>       |
| Interest rate gap                                     | <u>135,393</u>       | <u>145,086</u> | <u>774</u>   | <u>414</u>    | <u>-</u>    | <u>4,134</u> | <u>285,801</u> | <u>23,721</u>  |

| 2016  | Non-interest-bearing | Up to 1 month  | 1 - 3 months | 3 - 12 months | 1 - 5 years  | Over 5 years | Total          | Fixed interest |
|---|----------------------|----------------|--------------|---------------|--------------|--------------|----------------|----------------|
|   | HRK '000             | HRK '000       | HRK '000     | HRK '000      | HRK '000     | HRK '000     | HRK '000       | HRK '000       |
| Loans and receivables                                 | 48,447               | -              | 1,023        | 1,812         | 1,155        | 4,765        | 57,202         | 23,958         |
| Trade and other receivables                           | 277,565              | (21)           | -            | -             | -            | -            | 277,544        | -              |
| Financial assets at fair value through profit or loss | 62,993               | -              | -            | -             | -            | -            | 62,993         | -              |
| Cash and cash equivalents                             | -                    | 213,375        | -            | -             | -            | -            | 213,375        | -              |
|   | <u>389,005</u>       | <u>213,354</u> | <u>1,023</u> | <u>1,812</u>  | <u>1,155</u> | <u>4,765</u> | <u>611,114</u> | <u>23,958</u>  |
| Borrowings  | 8,954                | -              | -            | -             | -            | -            | 8,954          | -              |
| Trade and other payables                              | 258,275              | -              | -            | -             | -            | -            | 258,275        | -              |
|   | <u>267,229</u>       | <u>-</u>       | <u>-</u>     | <u>-</u>      | <u>-</u>     | <u>-</u>     | <u>267,229</u> | <u>-</u>       |
| Interest rate gap                                     | <u>121,776</u>       | <u>213,354</u> | <u>1,023</u> | <u>1,812</u>  | <u>1,155</u> | <u>4,765</u> | <u>343,885</u> | <u>23,958</u>  |

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 27 Financial risk management (continued)

### (c) Price risk

The Company has insignificant exposure to debt securities price risk due to low investments and all classified on the balance sheet at fair value through profit or loss (investments funds).

### (d) Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. Significant risk is associated with a high level of customer finance receivables.

The internal directives to manage the credit risks have been tightened during 2015 with the implementation of updated credit management framework and implementation of credit evaluation tools to manage credit risks.

Credit Management function within the Treasury has been established to further assist the Company in managing its credit risk exposure.

New customers are only accepted on satisfactory completion of a detailed credit check of the customer and a review of the related country risk. Outstanding credit arrangements are monitored on a quarterly or annual basis depending on risk category. Impairment losses are calculated by discounting of receivables. Additionally, there is credit concentration risk as the Company has a significant portion of receivables outstanding from a small number of customers. As at 31 December 2017, the five largest customers represent 59% of total net trade receivables (2016: 48%). The Company considers that its maximum exposure to credit risk is reflected in the amount of trade receivables (Notes 12 and 15) and other receivables (Note 16), not impaired as doubtful receivables. Ageing analysis of these receivables is within the maturity analysis table shown further in this note.

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

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

The Company defines customer financing as any credit period longer than 179 days. The Company is working closely with Croatian Bank for Reconstruction and Development (HBOR) and partnership banks to secure risk mitigation.

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

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

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 27 Financial risk management (continued)

### (d) Credit risk (continued)

The following tables provide an ageing detail of current and overdue amounts in respect of all customer loans and receivables as at 31 December 2017.

| Table 1                           | Payment due date for total customer loans and receivables |                |                    |               |              |                |
|-----------------------------------|---|----------------|--------------------|---------------|--------------|----------------|
|                                   | Due balance   | Up to 3 months | 3 months to 1 year | 1 to 3 years  | Over 3 years | Total          |
|                                   | HRK '000  | HRK '000       | HRK '000           | HRK '000      | HRK '000     | HRK '000       |
| 2017                              |   |                |                    |               |              |                |
| Foreign receivables               | 520   | 65,448         | 26,476             | 52,331        | 5,580        | 150,355        |
| Domestic receivables              | 2,128   | 51,364         | 1,983              | 67            | -            | 55,542         |
| Receivables from related parties* | 4,670   | 173,985        | 9,614              | 1,551         | -            | 189,820        |
|                                   | <u>7,318</u>  | <u>290,797</u> | <u>38,073</u>      | <u>53,949</u> | <u>5,580</u> | <u>395,717</u> |

\*include non-current portion of domestic receivables in the amount of HRK 1,552 thousand

|                                  |               |                |               |               |              |                |
|----------------------------------|---------------|----------------|---------------|---------------|--------------|----------------|
| 2016                             |               |                |               |               |              |                |
| Foreign receivables              | 2,848         | 62,407         | 56,044        | 43,065        | 9,943        | 174,307        |
| Domestic receivables             | 1,761         | 57,860         | 2,877         | 523           | -            | 63,021         |
| Receivables from related parties | 8,027         | 78,870         | 4,827         | 2,400         | -            | 94,124         |
|                                  | <u>12,636</u> | <u>199,137</u> | <u>63,748</u> | <u>45,988</u> | <u>9,943</u> | <u>331,452</u> |

\*include non-current portion of domestic receivables in the amount of HRK 2,400 thousand

| Table 2                          | Ageing of total due customer loans and receivables |                    |              |              |               |
|----------------------------------|--|--------------------|--------------|--------------|---------------|
|                                  | Up to 3 months                                     | 3 months to 1 year | 1 to 3 years | Over 3 years | Total         |
|                                  | HRK '000   | HRK '000           | HRK '000     | HRK '000     | HRK '000      |
| 2017                             |  |                    |              |              |               |
| Foreign receivables              | 520  | -                  | -            | -            | 520           |
| Domestic receivables             | 2,067  | 61                 | -            | -            | 2,128         |
| Receivables from related parties | 3,419  | 971                | 195          | 85           | 4,670         |
|                                  | <u>6,006</u>                                       | <u>1,032</u>       | <u>195</u>   | <u>85</u>    | <u>7,318</u>  |
| 2016                             |  |                    |              |              |               |
| Foreign receivables              | 2,656  | 192                | -            | -            | 2,848         |
| Domestic receivables             | 1,677  | 84                 | -            | -            | 1,761         |
| Receivables from related parties | 6,750  | 1,040              | 120          | 117          | 8,027         |
|                                  | <u>11,083</u>                                      | <u>1,316</u>       | <u>120</u>   | <u>117</u>   | <u>12,636</u> |

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 27 Financial risk management (continued)

### (d) Credit risk (continued)

|                                  | Due balance<br>HRK '000 | Up to 3<br>months<br>HRK '000 | 3 months<br>to 1 year<br>HRK '000 | 1 to 3 years<br>HRK '000 | Total<br>HRK '000 |
|----------------------------------|-------------------------|-------------------------------|-----------------------------------|--------------------------|-------------------|
| 2017                             |                         |                               |                                   |                          |                   |
| Foreign receivables              | 520                     | 13,256                        | -                                 | -                        | 13,776            |
| Domestic receivables             | 2,128                   | 1,068                         | 47                                | -                        | 3,243             |
| Receivables from related parties | 4,670                   | 162,583                       | 1,508                             | -                        | 168,761           |
|                                  | <u>7,318</u>            | <u>176,907</u>                | <u>1,555</u>                      | <u>-</u>                 | <u>185,780</u>    |
| 2016                             |                         |                               |                                   |                          |                   |
| Foreign receivables              | 2,848                   | 19,357                        | 624                               | -                        | 22,829            |
| Domestic receivables             | 1,761                   | 13,145                        | 2,007                             | -                        | 16,913            |
| Receivables from related parties | 8,027                   | 68,745                        | 4,827                             | -                        | 81,599            |
|                                  | <u>12,636</u>           | <u>101,247</u>                | <u>7,458</u>                      | <u>-</u>                 | <u>121,341</u>    |

|                                  | Up to 3<br>months<br>HRK '000 | 3 months<br>to 1 year<br>HRK '000 | 1 to 3 years<br>HRK '000 | Over 3 years<br>HRK '000 | Total<br>HRK '000 |
|----------------------------------|-------------------------------|-----------------------------------|--------------------------|--------------------------|-------------------|
| 2017                             |                               |                                   |                          |                          |                   |
| Foreign receivables              | 520                           | -                                 | -                        | -                        | 520               |
| Domestic receivables             | 2,067                         | 61                                | -                        | -                        | 2,128             |
| Receivables from related parties | 2,487                         | 635                               | 194                      | -                        | 3,316             |
|                                  | <u>5,074</u>                  | <u>696</u>                        | <u>194</u>               | <u>-</u>                 | <u>5,964</u>      |
| 2016                             |                               |                                   |                          |                          |                   |
| Foreign receivables              | 2,656                         | 192                               | -                        | -                        | 2,848             |
| Domestic receivables             | 1,677                         | 84                                | -                        | -                        | 1,761             |
| Receivables from related parties | 3,635                         | 294                               | 84                       | -                        | 4,013             |
|                                  | <u>7,968</u>                  | <u>570</u>                        | <u>84</u>                | <u>-</u>                 | <u>8,622</u>      |



Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 27 Financial risk management (continued)

### (e) Liquidity risk

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

The Company has a revolving credit facility with our core banks should an extraordinary liquidity need arise. As at 31 December 2017, the facility remained untapped.

| 2017                        | Up to 1<br>month | 1 - 3<br>months  | 3 - 12<br>months | 1 - 5<br>years | Over 5<br>years | Total          |
|-----------------------------|------------------|------------------|------------------|----------------|-----------------|----------------|
|                             | HRK '000         | HRK '000         | HRK '000         | HRK '000       | HRK '000        | HRK '000       |
| Loans and receivables       | 761              | 3,336            | 11,472           | 62,931         | 4,374           | 82,874         |
| Trade and other receivables | 222,685          | 98,393           | 23,456           | 700            | -               | 345,234        |
| Current financial assets    | 84,520           | -                | -                | -              | -               | 84,520         |
| Cash and cash equivalents   | 144,838          | -                | 248              | -              | -               | 145,086        |
|                             | <u>452,804</u>   | <u>101,729</u>   | <u>35,176</u>    | <u>63,631</u>  | <u>4,374</u>    | <u>657,714</u> |
| Borrowings                  | -                | -                | -                | 8,378          | -               | 8,378          |
| Trade and other payables    | 48,561           | 283,510          | 900              | 6,843          | -               | 339,814        |
|                             | <u>48,561</u>    | <u>283,510</u>   | <u>900</u>       | <u>15,221</u>  | <u>-</u>        | <u>348,192</u> |
| Maturity gap                | <u>404,243</u>   | <u>(181,781)</u> | <u>34,276</u>    | <u>48,410</u>  | <u>4,374</u>    | <u>309,522</u> |

| 2016                        | Up to 1<br>month | 1 - 3<br>months | 3 - 12<br>months | 1 - 5<br>years | Over 5<br>years | Total          |
|-----------------------------|------------------|-----------------|------------------|----------------|-----------------|----------------|
|                             | HRK '000         | HRK '000        | HRK '000         | HRK '000       | HRK '000        | HRK '000       |
| Loans and receivables       | 10               | 5,071           | 13,853           | 57,946         | 4,280           | 81,160         |
| Trade and other receivables | 158,995          | 43,459          | 74,306           | 784            | -               | 277,544        |
| Current financial assets    | 62,993           | -               | -                | -              | -               | 62,993         |
| Cash and cash equivalents   | 213,375          | -               | -                | -              | -               | 213,375        |
|                             | <u>435,373</u>   | <u>48,530</u>   | <u>88,159</u>    | <u>58,730</u>  | <u>4,280</u>    | <u>635,072</u> |
| Borrowings                  | -                | -               | -                | 8,954          | -               | 8,954          |
| Trade and other payables    | 164,208          | 79,605          | 5,719            | 8,743          | -               | 258,275        |
|                             | <u>164,208</u>   | <u>79,605</u>   | <u>5,719</u>     | <u>17,697</u>  | <u>-</u>        | <u>267,229</u> |
| Maturity gap                | <u>271,165</u>   | <u>(31,075)</u> | <u>82,440</u>    | <u>41,033</u>  | <u>4,280</u>    | <u>367,843</u> |

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 27 Financial risk management (continued)

### (f) Fair value estimation

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

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

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

|   | Carrying amount | Fair value     | Unrecognised gain/(loss) | Carrying amount | Fair value     | Unrecognised gain/(loss) |
|---|-----------------|----------------|--------------------------|-----------------|----------------|--------------------------|
|   | HRK '000        | HRK '000       | HRK '000                 | HRK '000        | HRK '000       | HRK '000                 |
|   |                 |                | 2017                     |                 |                | 2016                     |
|   |                 |                |                          |                 |                |                          |
| Loans and receivables                                 | 82,874          | 82,366         | (508)                    | 81,160          | 82,617         | 1,457                    |
| Trade and other receivables                           | 345,235         | 345,217        | (18)                     | 277,544         | 277,472        | (32)                     |
| Financial assets at fair value through profit or loss | 84,520          | 84,520         | -                        | 62,993          | 62,993         | -                        |
| Cash and cash equivalents                             | 145,086         | 145,086        | -                        | 213,375         | 213,375        | -                        |
| Borrowings  | (8,378)         | (8,378)        | -                        | (8,954)         | (8,954)        | -                        |
| Trade and other payables                              | (339,814)       | (339,814)      | -                        | (258,275)       | (258,275)      | -                        |
|   | <u>309,523</u>  | <u>308,997</u> | <u>(526)</u>             | <u>367,843</u>  | <u>369,228</u> | <u>1,425</u>             |

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

Notes to the Financial Statements of Ericsson Nikola Tesla d.d. (continued)

## 27 Financial risk management (continued)

### (f) Fair value estimation (continued)

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

|                       | 2017  | 2016  |
|-----------------------|-------|-------|
| Loans and receivables | 0.80% | 1.40% |

### (g) Capital management

The Company's objectives when managing capital are:

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

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

The Company monitors capital using the statutory minimum capital requirement. Shareholders' equity is disclosed in Note 19 to the financial statements.