
COMPANY POSITION REPORT

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

Dear shareholders,

Despite all the challenges in the development of a modern civilization, ICT continues to change business performance and peoples' lives and have even more significant impact on the society and the environment. Recognizing the needs of modern people for permanent use of innovative ICT solutions, as well as the need for sustainable development of the society; the industry, which we operate in, has been quickly modulating the new communications era that takes us to the networked society. At Ericsson Nikola Tesla, we share the vision of a networked society, due to our awareness of its impacts on human life, productivity and sustainable development.

Although exposed to a demanding market environment, and negative economic trends in Croatia and other markets, Ericsson Nikola Tesla ended the year 2012 with excellent business results. Sales revenue is 64% higher year-over-year, as a result of a significant increase of revenue in CIS and Ericsson markets. Simultaneously, sales in domestic markets increased slightly year-over-year, while other export markets decreased as a result of negative economic trends, political turmoil and postponed customer investments.

I would like to point out that in 2012 we strengthened our market share and implemented a few strategically important projects and contracts, respectively, which show that continuous market presence and listening to the needs of our customers combined with technological leadership and competent expert resources bring the results. The revenue structure by markets is significantly changed in favor of export markets. In total sales revenue the domestic market share is 14%, and the export reached a record high 86%.

In the Russian market, we successfully implemented a demanding project on 2G and 3G mobile networks for Rostelecom. With a new mobile network, Rostelecom becomes a convergent operator, which will provide a whole package of convergent services to its users in the field of information and telecommunications in mobile and fixed networks across the Russian Federation. This is the biggest deal the Company signed in the last few years. However, it is unrealistic to expect that such a large single deal with an individual customer happens each year.

In the domestic market Ericsson Nikola Tesla became the only supplier of the cutting edge radio access network to Vipnet and thus consolidated its position as the leading supplier of the cutting edge solutions. Furthermore, a multi-year agreement concerning the implementation of IP/MPLS network backbone was signed with Hrvatski Telekom (T-HT), which is the foundation for future business performance of T-HT as a convergent operator and a way to „all-IP“ environment. In the area of ICT solutions for business segment industry and society, we made deals on maintenance and upgrade of the Central Information Healthcare System in the Republic of Croatia.

In the market of Bosnia and Herzegovina, we made an agreement with BH Telecom on mobile network extension, related to 2G/3G technologies, which is, at the same time, a preparation for the transition to LTE technology. By investing additional efforts, in order to strengthen our presence in a neighboring market of Bosnia and Herzegovina, and improve our business performance as well, we established a company ETK BH d.o.o., fully owned by Ericsson Nikola Tesla. Consequently Ericsson Nikola Tesla submits a consolidated financial report as of 2012.

The major part of our activities and the related revenues refer to research and development and other expert activities, where the company permanently expands its portfolio and responsibilities and our experts are engaged in numerous demanding projects. The performance of our Research & Development Centre in 2012 was evaluated as high by Ericsson R&D Operational Steering Group. Bearing in mind the importance of this segment for the future of the entire Company, we shall going forward continue to put our maximum focus on this area in order to improve our competitiveness.

I would like to emphasize that our permanent focus on innovations gives excellent results. We have been recognized by the Ericsson Group for our quality, innovation processes and creativity of our experts, which is also confirmed by global awards won by our teams and individuals.

As a part of the Company reward and motivation program, we acquired additional 2375 Ericsson Nikola Tesla shares, intended for distribution to our employees.

In the year 2012, Ericsson Nikola Tesla achieved the following consolidated business results (data for 2011 in brackets):

- ✓ Sales revenue MHRK 1,913.3 (MHRK 1,165.8)
- ✓ Net profit MHRK 126.9 (MHRK 28)
- ✓ Strong cash flow from operating activities MHRK 298 (MHRK 134.8)
- ✓ Company's motivating culture and a strong employee engagement were confirmed by the annual employee opinion questionnaire (Dialog).
- ✓ The Customer satisfaction was confirmed by the annual customer survey.

In brief, in 2012 we achieved a significant improvement of almost all key performance indicators also mirrored in a stable balance sheet. With the increase in revenue, net profit grew by 353% year-over-year. We also achieved a strong cash flow from operating activities. We have continued to invest in strategic projects and customers, developing competencies of our employees and strengthening our market position. Simultaneously, we had a strong focus on efficiency increase, cost reduction and risk management. Therefore, 2012 was a successful business year, which is an excellent precondition for future positioning, investment and development.

Business outlook

In the period to come, the telecom market will remain extremely dynamic. Mobile data traffic shows a significant growth due to the considerable increase in the number of mobile *smart* user devices, as well as due to the increased use of the Internet. Accordingly, further growth of fixed broadband access to xDSL technologies and also introducing high-speed technologies based on optics (FTT-x) is expected.

Mobile broadband access will continue a strong growth by further implementing the 3 and 3.5 generation of mobile technologies (HSPA, HSPA+), and in Croatia we expect a more intense implementation of LTE technology. Furthermore, we expect a more significant modernization of the existing mobile networks based on SRAN concept (Single Radio Access Network), which enables operators more efficient business performance and optimizing their costs.

In edge and core networks the transformation to “all IP” Next Generation Convergent Networks based on the IMS architecture will continue.

We also expect modernization of Operation Support System (OSS) and Business Support System (BSS) as well as IPTV platforms. Finally, this all will enable operators to provide a wide range of convergent services, regardless of the location or the user approach.

The implementation of ICT should be increased in the Industry and Society segment both in enterprise and state administration because of effects and benefits achieved by the development, implementation and usage of up to date ICT solutions and services.

The first steps in the area of m2m (machine-to-machine) communications are also expected, as well as gradual implementation of *cloud* solutions and business models based on them.

Considering mostly unchanged market environment, risks in business performance which marked the previous period still remain present. Therefore, by assessing the risks of Ericsson Nikola Tesla's business performance in 2013, hereby I list the following:

- ✓ Reduction and slow down of capital investments of operators and postponements of strategic investments in public and private sector
- ✓ The impact of the product and services mix on gross margin
- ✓ Strong competition among existing and new service providers, including IT companies entering the ICT market
- ✓ Consolidation among customers and competitors may have additional impact to prices of products and services
- ✓ Continuation of political uncertainty and instability on some markets
- ✓ Enlarged credit and commercial risk exposure in case of deterioration of our customers' financial conditions

- ✓ Negative impact of currency deviations on business results since the majority of our earnings have been achieved in EUR and USD
- ✓ Retaining highly skilled and best quality employees to stay competitive.

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

The strategy of Ericsson Nikola Tesla is focused on further strengthening of the position in domestic, Ericsson and export markets, on further expanding of the customer base, acquiring new responsibilities and offering the cutting edge solutions, products and services. The key factors to achieve this are technological leadership, development of new models that encourage permanent learning and development of innovations. ICT industry will continue to have an important role in business performance development and in the society in general. The introduction of new devices and applications results in greater user's expectations concerning the quality and network performance, which increases the demand for our technological solutions and services. Therefore, our strategic priorities are focused on the areas with a potential to grow, such as mobile broadband access, services and operational and business support systems. Strengthening profitability and reducing costs is still of utmost importance in our strategy.

It is quite certain that economic uncertainty and business challenges will mark 2013 as well. Therefore, we will be focused on a constant adjustment to technological and market conditions, as well as risk management. We shall continue to contribute to Ericsson's technological leadership, strengthen our relations to customers and all other partners, and shall invest into knowledge and competencies of our employees, remaining aware of the fact that this is what makes us recognizable in the market.

All other data, being an integral part of the annual Company report, pursuant to Article 250 (a) of the Company Act, can be found in the enclosed 2012 Annual Report, comprising of the General Report, Social Report, Consolidated Financial Statements as at December 31, 2012 incl. Auditor's report.

Gordana Kovačević

President
Ericsson Nikola Tesla d.d.

