

**OT - Optima  
Telekom d.d.  
Annual Report and  
Report for the 4<sup>th</sup>  
quarter of the  
Group for 2018**

**20  
18**

**Optima**  
TELEKOM



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# Corporate Governance and General Information

<b>SUPERVISORY BOARD</b>	Igor Vavro — CHAIRPERSON Ariana Bazala-Mišetić — DEPUTY CHAIRPERSON Ana Hanžeković — MEMBER Rozana Grgorinić — MEMBER Jelena Noveljić — MEMBER Blaženka Klobas — MEMBER Silvija Tadić — MEMBER Igor Radojković — MEMBER Suzana Čepl — MEMBER — EMPLOYEE REPRESENTATIVE
<b>BOARD OF DIRECTORS</b>	Boris Batelić — CHAIRMAN Irena Domjanović — MEMBER Tomislav Tadić — MEMBER
<b>IBAN</b>	HR3023600001101848050 Zagrebačka banka d.d. Zagreb Commercial Court of Zagreb
<b>OIB</b>	36004425025
<b>MBS</b>	040035070
<b>MB</b>	0820431
<b>SHARE CAPITAL</b>	
<b>AMOUNT</b>	694.432.640,00 HRK
<b>NUMBER OF SHARES</b>	69.443.264, nominal value of HRK 10.00 each

# Optima Telekom Group Members and Regional Centers

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- OT-Optima Telekom d.o.o, Ulica 15. maja  
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# I. **Management Report**

# Introduction

## I.1

In 2018 business year, being duly authorised by the Shareholders' General Meeting and based on Decision of Commercial Court in Zagreb from August 1st 2017, the Company has completed the admission of 5,886,456 shares to the official market of the Zagreb Stock Exchange. The said admission of shares is a result of the implementation of the General Meeting's decision on the increase of share capital, with the purpose of completing the merger of H1 TELEKOM d.d. (acquired company) with Optima Telekom d.d. (acquiring company).

Based on the authorisation contained in the aforementioned Decision of the General Meeting, the Board of Directors took all the necessary steps based on which the CDCC executed the corporate action of converting common stock of the Company marked as OTE-R-C, ISIN: HROPTERCO009, and reported to the public accordingly on 26 March 2018. After the conversion of shares, 69,443,264 common shares marked OTE-R-A, ISIN: HROPTERA0001 have been included in the depository, clearing and settlement services of the CDCC.

After the execution of the corporate action of converting the shares by the CDCC, on 27 March 2018 the Zagreb Stock Exchange rendered and published its Decision, class: UP/I-451-01/18-01/15, cons. no. 536-18-2, approving the admittance of 5,886,456 shares, having the nominal value of HRK 10.00 each, marked OTE, ISIN: HROPTERA0001, to the Official Market of the Zagreb Stock Exchange, and designated 29 March 2018 as the first day of trading with financial instruments.

By completing the conversion and the admittance of 5,886,456 newly issued shares to the Official Market of the Zagreb Stock Exchange,

the Company has completed all the activities envisaged in the General Meeting's Decision on the increase of share capital for the purpose of merging H1 TELEKOM d.d.

Pursuant to the provisions of the Company's Statute and the decision of the Board of Directors of 7 May 2018, the Company's regular General Meeting took place on 14 June 2018.

Just as in the period from the execution of the Settlement, the Company continues to duly perform all due obligations undertaken in the Pre-bankruptcy Settlement executed before the Commercial Court of Zagreb on 30 April 2014, case reference Stpn-354/13, and reports to the public regarding the said actions in accordance with the Financial Operations and Pre-bankruptcy Settlement Act via FINA's website, [www.fina.hr](http://www.fina.hr). Because of the merger with H1, the Company has become the universal successor of all the rights and obligations of H1, thereby assuming the position of the debtor in the pre-bankruptcy settlement approved by the Commercial Court of Split, case reference Stpn-74/2014, having been duly executed on 16 December 2014. The Company reports to the public regarding its actions in accordance with the Financial Operations and Pre-bankruptcy Settlement Act via FINA's website, [www.fina.hr](http://www.fina.hr).

Apart from publications on Fina's website regarding the issues related to the implementation of the Pre-bankruptcy Settlement, the Company is informing the public on the fulfilment of obligations in a timely and transparent fashion in accordance with the relevant laws and regulations in the field of capital markets.

## I.2

## Statement by the Chairman of the Board

“It is with great pleasure that I can say that the business data of Optima Telekom Group at the end of 2018 continue to show good results and positive business trends. Revenues have increased by 10.5% while operating profit before special items (EBITDA) went up by 19.9%. At the level of the fourth quarter, Optima Telekom Group improved the EBITDA before special items by as much as 50.4% compared to the previous year.

Along with the synergy contribution of the H1 merger, these results were influenced by the sales results in all the telecommunications segments important to the Company, towards which we specifically targeted our sales and marketing activities: internet, multimedia and ICT solutions and services. In the offers segment, we continued to launch innovative solutions on the market in the previous year as well. After a particularly successful package deal with no contractual obligations at the price of the package under a contractual obligation, recommendation program and introducing gift cards, last year Optima Telekom was once again the first to offer the market the DUoiPol package. This is a service which provides advanced functionalities of television such as the recorder, return to beginning, rewind to customers who feel that the land channels are not enough.



Boris Batelić,  
Chairman of the Board

The previous year was also characterized by investments into network infrastructure, where significant funds went into the enlargement of our own optical fiber network, especially in areas under special state care.

In the future, we anticipate the challenging struggle to continue, because the telecommunications market in Croatia is highly competitive. Our objective, first and foremost, is a satisfied customer. This is why Optima Telekom continues to invest into optimization and increasing company efficiency as well as quality of services and products.



# Market Overview

## I.3

### Fixed Telephony Market

The fixed telephony market in Croatia continues to have a negative trend. It is expected that revenues and traffic will continue to decline in the future, given the growing trend in the number of users and connections in the mobile communications network, and due to the growing availability of alternative, free, so called VoIP communications platforms.

In the third quarter of 2018, the total outbound traffic (in minutes) of all fixed public communications network operators decreased by 7.0%, while revenues remained the same.

The total outbound traffic (in minutes) of all fixed public communications network operators in the third quarter of 2018, when compared with the third quarter of 2017, is lower by 10.0%, while retail revenues recorded a significant decline of 12.0% over the same period.

### Broadband Access Market

In the third quarter of 2018, there was an increase in the use of broadband Internet access services via fixed networks. Compared to the second quarter of 2018, the number of broadband access connections via fixed networks increased slightly in the third quarter, by 0.3%, while revenues increased by 0.8%, mostly as

a result of increased investments into optical infrastructure.

Compared to the third quarter of the previous year, the number of broadband access connections via fixed networks increased by 2.6% in the second quarter of 2018. In the same period, revenues increased by 0.6% as a result of expanding of the portfolio of Internet services and additional payments for maximum speeds due to the growing request for higher speeds trend.

Predictions are that this market will continue to grow at a stable growth rate.

### IPTV Market

The Internet Protocol Based Television (IPTV) market continues on its mildly rising path. The total number of connections in the third quarter of 2018 increased by 0.2% compared to the previous quarter.

Comparing the total number of connections between the third quarter of 2018 and the third quarter of 2017, it shows a 1.2% increase at the annual level.

Considering the constant declining trend in the users of digital land TV signal, there is a potential for growth in the number of IPTV users.

# Economic Environment

## I.4

According to previously published indicators, during the first half of 2018 the GDP at the annual level was increased by 2.7% due to the influence of personal consumption. The third quarter was characterized by an unfavorable trend in industrial production, so that the estimated growth rate remains under 3.0%, and on this basis the European Commission kept its estimate at 2.8% and for the following year an increase by 0.1 percentile. According

to data from 2017, the export of goods was at 65%, while the "export" towards EU member states consists of 70% of services, mostly in tourism. In its latest estimates, the EU is pessimistic regarding EU growth. For this year it reduced the estimate from 2.3% to 2.1%, and for the following year from 2.0% to 1.9%. Lower growth estimates are in line with realized trends. The GDP increased by 0.2% compared to the previous quarters and compared to the

previous two quarters by 0.4% and 0.5%. At the annual level, the GDP growth slows down, so after 2.3% in the first and 2.1% in the second, the growth slowed down by 1.9%.

In September of this year the number of unemployed persons went down by 3.5 thousand compared to the previous month. The unemployment numbers have reached a record low (130 577). For the third year in a row, the number of unemployed persons registered with the HZZ has decreased in September, immediately after the main tourist season. The main reason for this is the reduced pressure on the employment office, i.e. less workers registered with the HZZ. The increase in demand on the labour market is still extremely high: according to the ovi indeks of the Zagreb Economic Institute, at the annual level, the demand was 24.4% higher in September (29.4% higher in the first nine months), and the number of job openings at the HZZ was 8.1% higher (3.4% in the first nine months). The conclusion is that the unemployment rate is a consequence of the discrepancy between the offer and demand. Albeit low, the unemployment rate is still high compared to other EU member states.

The salary growth tendency continued in August, specifically by 0.9% in gross salaries and one percent in net salaries. This also continued the tendency of higher increases of gross salaries compared to net salaries. The net salary in October was two percent higher compared to October of the previous year, and the gross salary went up by 2.6%. In the first eight months of this year, the average monthly gross salary for employees in companies amounted to HRK 8,448, which is nominally 5.3%, and actually 3.6% higher than in the first eight months of 2017. Also, the average monthly net salary per employee amounted to HRK 6,264, which is nominally 4.6% and actually 3.0% higher compared to the same period of the previous year. The leading industries when it comes to the increase of net salaries are marketing (advertising and propaganda) and market research with 16.9%, while the biggest reduction in average salaries happened in the production of basic pharmaceuticals (by 5.6%). The continued growth contributes to the increase of available income and households' consumption. Additional tax reforms open the possibility

for the present tendencies to continue if the tax relief is used for the increase of salaries.

The period of a stable and relatively high HRK exchange rate has continued in September and October. Since the beginning until the end of September, the Croatian Kuna strengthened compared to the Euro by 0.1%, and during October it weakened by 0.3%. There were more oscillations towards the us Dollar, as a consequence of the Euro's weakening compared to the us Dollar. In September and October, the Euro weakened by 2.9% compared to the us Dollar. The greatest influence of the Dollar strengthening compared to the Euro was Italy's decision to accept a significantly higher budget deficit than the agreed, and subsequent negotiations between that country and the European Commission. In the previous year, the average Euro exchange rate with the us Dollar at the annual level increased. There was a 6.3% growth in the first nine months. The Euro strengthened compared to other currencies as well, and the Kuna did accordingly.

The new Act on Enforcement on Monetary Funds entered into force on 4 August 2018, replacing the old one, adopted eight years ago. FINA's activities based on the new Act resulted in drastic changes in FINA statistics regarding the status of blocked individuals and their debts in the first month of its application (August). The total debt of private citizens was reduced by HRK 38 billion (principal + interest) in a month, and amounted to HRK 26.5 billion (out of which HRK 19.2 billion goes to principal claims) at the end of August. There were 43,992 citizens less with their accounts seized by FINA, and at the end of August there were 274,529 of them. As for business entities, because of FINA's activities based on the new Act, the debts of natural persons (tradesmen) were drastically reduced in the first month of its application, by as much as 67% (from HRK 5.2 to HRK 1.7 billion). There were no significant changes in the debts of legal entities, which continued to decrease at a slow rate. The trend of overall debt of business entities, after a greater decrease in August (by 32.6%), went back to being a slow decreasing trend (-3.0%) in September.

# Regulatory Environment

## I.5

In this reporting period, there were no significant changes in the regulation of the electronic communications market, i.e. no decisions were rendered by the Croatian Regulatory Authority for Network Industries (hereinafter: HAKOM).

However, in this reporting period HAKOM has commenced the procedure of regular analysis of the call origination on the public telephone network provided at a fixed location market (M2/2007), call termination on individual public telephone networks provided at a fixed location market (M1/2014) and voice call termination on individual mobile networks wholesale market (M2/2014). Final decisions in the aforementioned procedures should be rendered in the upcoming reporting periods. The same could have an impact on the Company's business, especially on the revenues from wholesale services and costs arising out of the use of wholesale services of call termination and origination provided by other operators.

It is worth noting that HAKOM had previously, within the procedure of regular market analysis, finalized the procedure and rendered a final decision regarding the access to the public telephone network at a fixed location

for residential and non-residential customers (M1/2007), whereby Optima, as a company controlled by HT, was imposed with appropriate regulatory obligations of price control and cost accounting. Thus the Company is still obligated to carry out the margin squeeze test for the access service, regardless of whether the same is provided independently or as a part of a package including other electronic communications services, in accordance with the document "Margin Squeeze Test Methodology". Because of the said obligation, the Company is not free to create its offers and has a limited market performance.

The same regulatory obligation was imposed on the Company in the wholesale local access at a fixed location market (M3a/2014) and the wholesale central access at a fixed location for mass market products market (M3b/2014). HAKOM commenced regular market analysis procedures for these markets as well. Final decisions in the aforementioned procedures should be rendered in the upcoming reporting periods.

During this reporting period, there were no significant amendments to the laws and regulations in the field of electronic communications.

## I.6 Business Indicators and Segments

Number of Customers	31.12.2018	30.09.2018	31.12.2018/ 30.09.2018	31.12.2017	31.12.2018/ 31.12.2017
<b>Business</b>					
JGU	18.829	19.126	-1,6%	20.226	-6,9%
IPTV	1.894	1.984	-4,5%	2.070	-8,5%
Internet	16.939	17.094	-0,9%	17.571	-3,6%
Data	2.033	1.999	1,7%	1.674	21,4%
<b>Residential</b>					
JGU	174.555	178.499	-2,2%	192.491	-9,3%
IPTV	48.013	47.262	1,6%	47.885	0,3%
Internet	116.236	117.666	-1,2%	122.500	-5,1%

### a. Residential Sales Segment

With a view to constantly develop its customer base, in the fourth quarter of 2018 Optima Telekom continues to invest in sales and marketing activities. Thanks to this, Optima Telekom has been able to maintain revenue stability in an extremely competitive environment.

Stability of the internet customer base and revenues in the fourth quarter of 2018 was greatly a result of focused efforts in marketing activities aimed at solely Internet services and the combination of Internet, telephone and television services throughout the said period. At the quarterly level, compared to the fourth quarter of the previous year, in the fourth quarter of 2018 Optima Telekom has recorded a 0.1% increase in Internet revenues, with a decrease in the number of customers by 5.1%. Compared to the third quarter of 2018 in this segment, there was a 1.0% revenue decrease, with a 1.2% decrease in the number of custo-

mers. The request for higher internet speeds trend continues, and thus Internet revenues increase. Optima Telekom's indicators at the level of the whole year in 2018 show a 17.1% revenue increase compared to the previous year, despite the 9.4% overall base decrease.

Traditionally, Optima Telekom has achieved good results in the segment of IPTV residential customers.

At the level of the last two quarters, in the IPTV segment Optima Telekom has achieved a 0.9% revenue increase in the fourth quarter of 2018, accompanied by a simultaneous 1.6% increase in the number of IPTV customers. In the fourth quarter of 2018, Optima has recorded a 2.9% revenue increase compared to the same quarter of the previous year, accompanied by a mild, 0.3% increase of the customer base. Comparing the results at the level of the whole year, in 2018 Optima Telekom has had a 17.1% increase in IPTV revenues compared to

the previous year. Positive trends in the IPTV segment are the result of the great potential of IPTV penetration in the Croatian market which Optima Telekom used by placing unique offers on TV packages.

National trends in the segment of residential customers of the fixed public voice service reflect on the trends within Optima Telekom. Observing the ratio between the fourth quarter of 2018 and the third quarter of 2018, the fourth quarter of 2018 ends with a 2.2% decrease in the number of residential customers of the public voice service and a 2.0% decrease in respective revenues in the same period. Indicators at the level of the whole year show a 2.8% decrease in revenue and 9.3% decrease in customer base in 2018, compared to the previous year.

Comparing the fourth quarter of 2018 and the fourth quarter of 2017, the number of public voice service customers decreased by 9.3%, accompanied by a 13.2% revenue decrease. The negative trend consequence is in line with the national market trend of decreasing the number of customers of communication services in fixed networks, which in turn causes the development and increased public availability of alternative VoIP wireless communication platforms.

## **b. Business Sales Segment**

In business sales the key activities of all sales channels in the fourth quarter of 2018, much like in all of 2018, were aimed at increasing the influx of new connections, extending the contracts with the existing corporate customers, migrating the H1 service package customers to the Optima Telekom system and network, and the sales of ICT solutions and services portfolio. During the fourth quarter a new organization was started with an emphasis on excellence in providing support for corporate customers in all segments.

In the fourth quarter of 2018 there was great focus on the activation of services agreed in major contracts in the key business customers segments, and the first revenue effects of nearly HRK 1 million have been achieved. In the public voice service segment we had a 1.2% decrease in revenue compared to the third quarter of 2018, and a 6.5% decrease compa-

red to the last quarter of the previous year. Comparing the fourth quarter of 2018 with the same period of the previous year, we can see a 6.9% decrease in the number of connections, while compared to the third quarter of 2018, we had a 1.6% decrease. The said decrease is a result of migration to more advanced solutions and packages, as well as the substitution of the fixed voice service with the voice service in mobile networks and the decreasing trend in the use of minutes of the public voice service. The total yielded revenues from public voice services is at the same level compared to 2017 because of the impact of the acquired company H1.

In the broadband Internet access segment, we had a 2.4% revenue increase compared to the fourth quarter of the previous year, while the increase compared to the third quarter of 2018 amounted to 0.9%. Compared to the fourth quarter of the previous year, we had a 3.6% decrease in customer base, while the decrease is 0.9% compared to the third quarter of 2018.

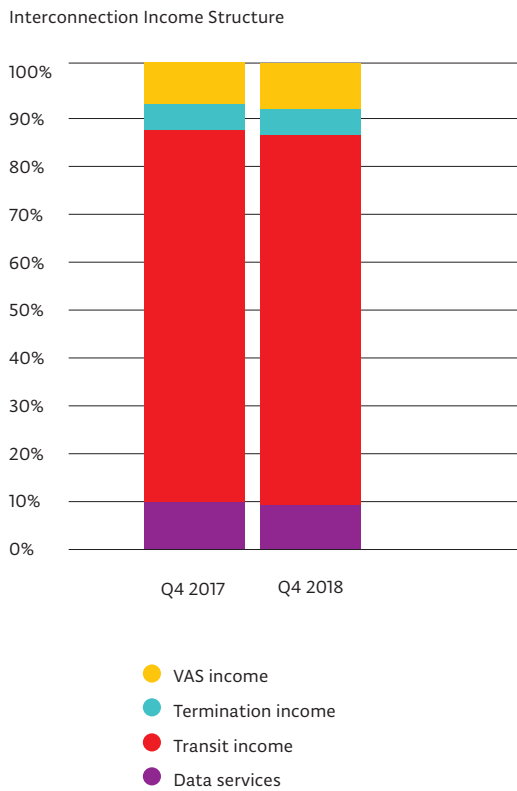
At the annual level, we have recorded a 15.4% revenue increase due to the impact of the acquired company H1 and the growth in sales of Internet services with higher capacities.

In the data services segment, in the fourth quarter of 2018 we have recorded a 21.4% customer base increase compared to the same quarter of the previous year, accompanied by a 4.2% revenue increase, which is a result of intense sales activities. The said increase in the number of data connections is a result of increased perception of customers who recognized the advantages of contracting private data services with the telecommunications services provided directly.

In the same segment, there was a 1.7% increase in the number of connections compared to the previous quarter, accompanied by a 1.7% revenue increase.

In this segment, there is still pressure from the competition on the prices of services in the segment of medium and large business customers.

In 2018 there was a robust increase in ICT revenues which went up to HRK 9.4 million, while in 2017 revenues amounted to HRK 2 million. The result was achieved due to a strong focus on the sales of ICT solutions and services and quality cooperation achieved with ICT par-



Data Source: Company's business records

tners, where we responded to market requests accordingly.

In 2018, data services revenues remained at the same level as in the previous year, primarily as a consequence of the merger of H1 Telekom, which fully made up for the loss of revenue from wholesale data services in the OT business field, which was caused in 2018 by the outflow of services caused by increased consolidation in the market (primarily by the VIPnet's acquisition of Metronet, where Optima lost a part of the services it offered to VIPnet and Metronet).

The revenues from transit of voice services in 2018 also remained at the same level as in 2017. In the field of termination, revenues were 4.1% higher in 2018 compared to 2017. This positive trend is a result of the customer base increased caused by the merger of H1 Telekom.

VAS services revenues increased by 11.3% compared to the same period of the previous year. VAS service revenue increase is a result of the merger of H1 Telekom and VAS operators who

provided their services using the H1 Telekom network, as well as the strengthening of the activities of VAS operators in the Optima Telekom's network.

### c. Infrastructure, Optical Fiber Network and Internal Services Development

#### Voice Networks

During 2018, voice traffic for six international operators has been migrated, along with the connection of two new national operators via the IP/SIP IC connections to the SBC-IC (Session Border Controller – Interconnection) systems.

The integration of all voice functions of the new UC (Unified Communications) Soft Switch system into the core of Optima's voice network has been completed, and the system was put into production by connecting new business customers of the Optima LAN used service to the new UC soft-switch. The integration of additional functionalities of the new UC soft-switch system was also completed, specifically the self-care web portal and softphone applications.

In 2018, a new database cluster has been implemented for the internally developed class 5 NGN switchboards that Optima uses to provide voice services to residential customers and small business customers, as well as business customers of the "business trunking" service, which achieved multiple redundancy and insured uninterrupted availability of the respective database.

H1 integration. In 2018 voice traffic towards the H1 Telekom network was aggregated through the Optima IP/SIP IC connections for the two remaining national operators, as well as the voice traffic of H1 CPS/WLR customers.

#### Data Networks

VDSL access network. After a more significant increase in the number of VDSL access interfaces on the ULL (Unbundled Local Loop) nodes in 2016 and 2017, in 2018 work was done on expanding the existing capacities. In this vein, the number of active VDSL interfaces at the end of 2017 was 17,500, and at the end of 2018, 22,350, which represents a 28% increase in the number of VDSL interfaces.



IP/MPLS core network. Further capacity upgrades were made and the level of quality was raised, i.e. the level of network availability through upgrading the MPLS (Multiprotocol Label Switching) routers. During the first quarter capacities to central nodes in Split, Rijeka and Zadar were increased, as were the inter-local nodes in Karlovac, Samobor, Prelog, Požega, Nova Gradiška, Novska, Popovača, Ivanić Grad, Dugo Selo, Krk, Pag, Gospić, Vrbovec and Križevci. During the second quarter capacities to the nodes in Jastrebarsko, Slatina, Virovitica and Zaprešić were increased and additional consolidation of former H1 nodes was carried out. By the end of 2018 capacities to nodes in Knin, Sinj, Zaprešić, Zabok, Krapina and Varaždin were increased as well.

Internet core network. The 10GE telecommunications connections at the relation OT Buzin - HT Megatrend were reconnected to increase redundancy of the existing interconnection capacities. In order to broaden the capacities of the Internet core network, the tender by invitation was competed in the third quarter and the system offered by the manufacturer Cisco was selected as the best solution, to be followed by the integration of new systems. OT-Optima Telekom currently has an agreed access capacity to the public Internet network (upstream) with the capacity of 40Gb/s. Considering the anticipated 20-25% traffic increase in the following year, during the fourth quarter a tender was carried out for broadening the capacity to 60 Gb/s, which is expected to be realized in the first quarter of 2019.

H1 core network integration. In the first quarter of 2018, further consolidation of the H1 and Optima core networks continued. Thus H1 nodes in Bjelovar, Gospić, Kutina and Split were reconnected so that all traffic would go through Optima's network. During the second quarter, work was done on the reconnection of Koprivnica, Čakovec and Zadar. During the third quarter the reconnection of lines to the nodes in Karlovac, Duga Resa, Vukovar and Đakovo was completed. During the fourth quarter, the remaining towns and cities were reconnected: Imotski, Metković, Šibenik, Zaprešić, Zabok, Krapina, Umag, Poreč, Pula and Rijeka whereby the H1 Telekom core network was entirely reconnected to Optima's core network.

ACS system – System for automatic configuration of terminal devices – as a system upgrade, OT-Optima telekom commenced the process of replacing the existing ACS system. A tender by invitation was organized and Axiros GmbH was selected as the highest-quality bidder. In the third and fourth quarter the integration of ACS systems is being carried out, and their full production is anticipated in the first quarter of 2019.

### **Optical Fiber Networks**

Optical infrastructure development, i.e. the construction of the individual optical fiber network in 2018 consisted mostly of the construction of optical feeds to our new end wholesale and retail customers, but also the construction of the core optical fiber network. More precisely, these are routes Bosiljevo-Grabrak, Duga Resa – Lipov Pesak and Generalski stol – Cerovac Barilovički, which were constructed to ensure a fast development of broadband networks in areas of special state care under the patronage of the Croatian Regulatory Authority for Network Industries, the reconstruction of a part of the Virovitica and Vukovar core optical fiber network, the reconstruction of the Split core optical fiber network concentrated around the TC nodes of Mejaši, Brda, Stobreč and Uglovnica, as well as the reconstruction of parts of the Pula and Pazin core optical fiber network.

In numbers, we are talking about 171.8 km of new optical fiber network, out of which 42.9 km represent the core optical fiber network and 129 km represent the access optical fiber network consisting of the construction of 404 new optical feeds.

Most feeds have been built in Northern Croatia (236 feeds), followed by the South (76 feeds), West (59 feeds) and Eastern Croatia with 33 optical feeds.

### **Internal Application Development**

A new Sports Programs Package was developed on the IPTV platform and the support for the "DuoIPol" package, which enables the renting of a group of TV programs for a certain period for the first time.

The 3G backup project has been realized, which provides business users with a more robust and reliable service. Backup for the sales of devices/goods has been implemented along-

gside existing services, thus broadening the offer of Optima Telekom.

The processes for successful migration of H1 Duo customers have been automated, with the possibility to keep existing modems, which resulted in significant savings in the migration of customers.

The first version of the new tool for controlling network devices has been developed to make the repairs of malfunctions easier both for technicians in the field and the colleagues in the call center.

The migration of existing servers to newly acquired, top of the line virtualization servers has commenced.

This doubled the capacity of virtual machines where the activities of Optima Telekom are performed.

The provisioning system has been upgraded to support DSLAM devices manufactured by ZTE, which fulfilled the precondition for integration of H1 collocations.

The preparation was made for a new customer analytics system designed to provide us with transparency in our work, better communication with customers, optimized and controllable debt recovery activities.

All Optima Telekom systems were upgraded so as to enable the collection and management of consents in accordance with the GDPR.

### **Power Systems**

Through the project of replacing batteries in Optima's network nodes with a view to ensure the system's autonomy in the event of an electric grid fallout, during the fourth quarter 120 batteries have been replaced at 21 locations.



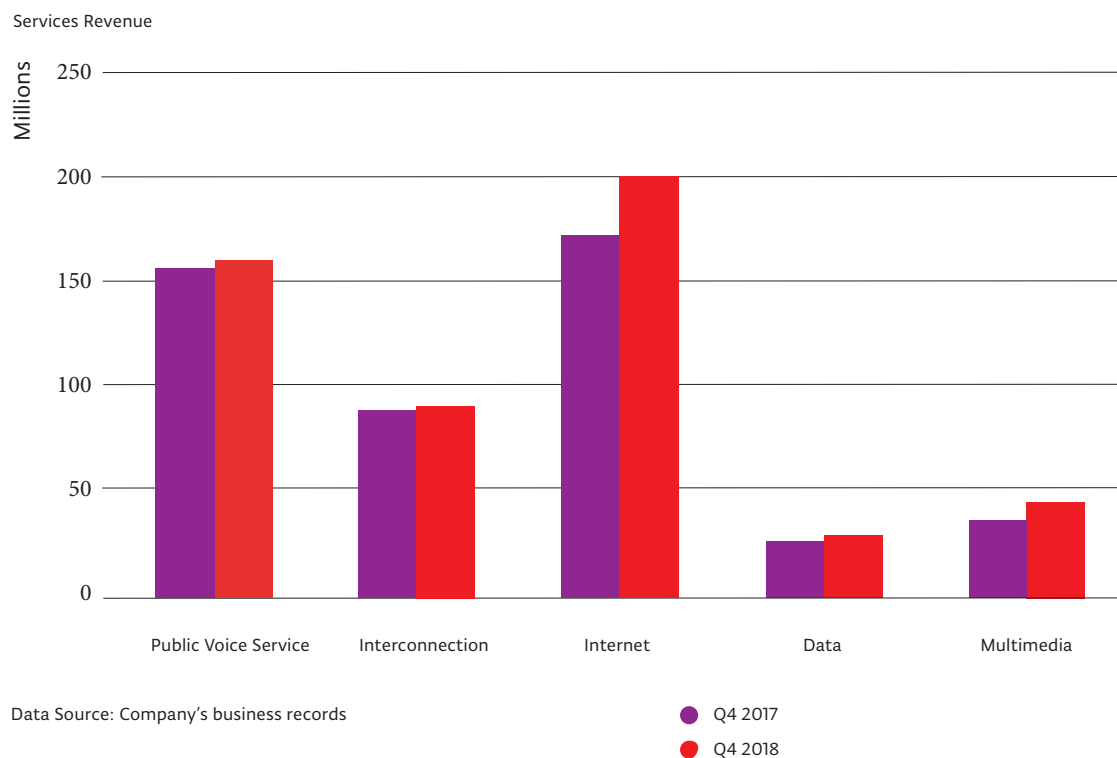
# Financial Results of the Group

I. 7

Summary ( <i>in tsd HRK</i> )	2017	2018	2018/ 2017	Q4 2017	Q4 2018	Q4 2018/ Q4 2017
Total income	495.091	547.144	10,5%	135.349	143.767	6,2%
Total expenses	389.684	420.626	7,9%	104.408	99.471	(4,7%)
EBITDA	105.407	126.518	20,0%	30.940	44.296	43,2%
One time items	6.290	7.409	17,8%	2.017	5.263	161,0%
<b>EBITDA before one time items</b>	<b>111.697</b>	<b>133.927</b>	<b>19,9%</b>	<b>32.957</b>	<b>49.559</b>	<b>50,4%</b>
<b>EBITDA margin (before one time items)</b>	<b>22,6%</b>	<b>24,5%</b>	<b>8,5%</b>	<b>24,3%</b>	<b>34,5%</b>	<b>41,6%</b>
Depreciation and impairment	150.343	91.817	(38,9%)	92.710	23.776	(74,4%)
Financial result (net)	(25.565)	(26.960)	5,5%	(6.604)	(7.763)	17,5%
Deferred taxes/Income taxes	11.613	(3.174)	(127,3%)	11.613	(2.507)	(121,6%)
Net profit/(loss)	(58.888)	4.567		(56.760)	10.250	

**a. Unconsolidated Results of the Company**

Summary ( <i>in tsd HRK</i> )	2017	2018	2018/ 2017	Q4 2017	Q4 2018	Q4 2018/ Q4 2017
Total income	482.173	546.161	13,3%	135.322	142.859	5,6%
Total expenses	376.988	420.671	11,6%	104.346	99.452	(4,7%)
EBITDA	105.185	125.490	19,3%	30.976	43.407	40,1%
One time items	4.057	7.409	82,6%	2.017	5.263	160,9%
<b>EBITDA before one time items</b>	<b>109.242</b>	<b>132.899</b>	<b>21,7%</b>	<b>32.993</b>	<b>48.670</b>	<b>47,5%</b>
<b>EBITDA margin (before one time items)</b>	<b>22,7%</b>	<b>24,3%</b>	<b>7,4%</b>	<b>24,4%</b>	<b>34,1%</b>	<b>39,7%</b>
Depreciation and impairment	146.116	91.530	(37,4%)	91.767	23.732	(74,1%)
Financial result (net)	(23.537)	(25.863)	9,9%	(6.701)	(7.800)	16,4%
Deferred taxes/Income taxes	11.613	(3.174)	(127,3%)	11.613	(2.507)	(121,6%)
Net profit/(loss)	(52.855)	4.923		(55.879)	9.368	



Compared to the previous year, the Group as achieved a 10.5% higher revenues and 19.9% higher EBITDA before special items. This is mostly owed to the merger of H1 Telekom and achieved synergies resulting from the merger. The same trends are present at the Group and Company level.

At the level of the fourth quarter, compared to the previous year, the Group has improved the EBITDA before special items by a significant 50.4%, considering that the fourth quarter of this year does not include the effects of the merger of H1 which had a negative impact on the EBITDA of the fourth quarter of 2017.

## b. Consolidated Revenue

Total services revenues in 2018 are 10.5% higher compared to the previous year, comparing mostly to the contribution of revenues of the merged H1 Telekom.

The revenue increase compared to the previous year was mostly caused by 18.6% higher multimedia revenues and 16.3% higher interner revenues, which are precisely the segments that are the focus of the Company's offer.

Public voice service revenues are higher by 1.1% compared to the previous year, owing to

the contribution of the merged H1 Telekom in 2018. However, the decreasing trend in revenues from public voice services is still present, thus continuing the general decreasing trend in the use of the public voice service, following the trends at the global level.

Data revenues in 2018 have increased slightly, by 0.1%, compared to the previous year, while interconnection revenues at the end of 2018 show a 1.1% increase compared to the results of the previous year.

## c. Earnings before Interest, Taxation and Depreciation – EBITDA

The consolidated EBITDA before special items amounts to HRK 133.9 million, being HRK 22.2 million higher compared to the previous year, mostly owing to the contribution of the merger of H1 Telekom. This contribution is reflected both in revenues and the achieved synergy effects on costs, which significantly contributes to the optimization of the overall business.

## d. Net profit/(loss)

Compared to the previous year, the net result has recorded a HRK 63.4 million increase, considering that during the pre-

	2018 (HRK 000)	share %
<b>General Investments</b>	<b>1.731</b>	<b>2%</b>
<b>Capital Technical Investments</b>	<b>83.706</b>	<b>98%</b>
ACCESS Network	34.712	40,6%
CORE Network	8.771	10,3%
Telecommunications Center	40.223	47,1%
<b>TOTAL</b>	<b>85.438</b>	<b>100%</b>

vious year, in the merger of H1 Telekom, the Company decreased the value of goodwill and trademark of the company H1.

### e. Capital Investments in 2018.

Consolidated capital investments in 2018 amounted to HRK 85.4 million. Out of this, HRK 34.7 million was invested into the development of the access optical fiber network, expanding the collocations network, user equipment for providing IPTV and internet services for residential users, as well as the equipment for business customers. HRK 8.8 million have been invested into the core network which was mostly used to further expand the core, while HRK 40.2 million have been invested into expanding the service portfolio.

### f. Risk Management

#### Currency Risk Management

The currency risk is the risk that the value of financial instruments will change due to exchange rate changes. The Company's highest exposure to currency risk arises out of long-term loans, denominated in foreign currencies and recalculated into HRK applying the relevant exchange rates as per the balance sheet date. Any exchange rate divergences shall be attributed to operating costs or recorded in the profit and loss account, but do not influence the cash flow.

#### Interest Risk

The Company's exposure to interest risk is not significant, given that the Company's liabilities have not been significantly agreed subject to variable interest rates.

The remaining assets and liabilities, including issued bonds, are not exposed to interest risk.

#### Credit Risk

The credit risk is the risk that the other party will fail to meet its contractual obligations arising out of potential financial losses of the Group. The Group does not have a significant credit risk concentration with contractual parties possessing similar characteristics and has adopted procedures it applies in buyer transactions. The Group receives sufficient collaterals, if necessary, as a means to mitigate the risk of financial loss due to unfulfilled obligations and offers no guarantees for third party liabilities.

#### Liquidity Risk Management

The Board of Directors has the responsibility for liquidity risk management and sets the appropriate framework for liquidity risk management, with a view to manage short-term, mid-term and long-term financing and liquidity requirements. The Company manages the liquidity risk by maintaining adequate reserves and credit lines, continuously comparing the planned and achieved cash flow and monitoring the receivables and liabilities due dates.

## Purchase of Own Shares

I. 8

As per 31.12.2018 the Company does not own its own shares.

## Statement Regarding the Application of the Code of Corporate Governance

II.

In accordance with articles 250a and 250b of the Companies Act, the Company has compiled the Annual Management Report on the Status and Business of the Company and the Group for 2018, which contains the Statement Regarding the Application of the Code of Corporate Governance.

In the course of its business, the Company strives to adhere to the highest possible extent to the recommendations of the Code of Corporate Governance as published on the website of Zagrebačka Burza d.d., taking into account all the circumstances and specificities of its business organisation.

The Company adheres to the recommendations in the Code of Corporate Governance with the exception of those provisions that cannot be considered practicable under the present circumstances:

- For those shareholders who are not able to vote in the General Meeting for whatever reason, the Company has not provided proxies obligated to vote according to their instructions, with no extra costs. The shareholders unable to vote personally choose their own proxy who is obligated to vote according to their instructions.

- There is no decision on dividend payment or dividend advance, considering that the dividend has not been paid in 2018.

- During the General Meeting, the shareholders were not given the opportunity to vote using modern communications technology because this has not been provided in the Statute.

- The work of the Supervisory Board is not regulated by special internal rules. The provisions of the Companies Act apply to the work of the Supervisory Board. However, the Supervisory Board has a Committee in place for the supervision of synergy measures, in accordance with the terms of the cleared concentration between Hrvatski Telekom d.d. and the Company. The work of the abovementioned Committee is regulated by the terms set

out in the Decision of the Croatian Competition Agency class: UP/I 034-03/2013-02/007, Cons. no. 580-06/41-14-096 of 19 March 2014 and the Decision of the same Agency class: UP/I 034-03/2013-02/007, Cons. No. 580-11/41-17-239 of 9 June 2017.

- The Supervisory Board does not have a majority of independent members, as defined in the Code's recommendations. All Supervisory Board members have been elected at the Company's General Meeting with adherence to the procedure of publishing candidacies, and the Workers' Council has appointed an employee representative in the Supervisory board.

- The Company does not have a drafted long-term succession plan, because the Company is investing in the education of its employees taking into account the business requirements.

- The Supervisory Board Members' right to remuneration for their work has been determined in a General Meeting decision, in a fixed monthly amount.

- The Company does not have agreements or contracts with Supervisory Board members, with the exception of the employment agreement of one of the Supervisory Board member – the elected employee representative, so the said agreement had not been pre-approved by the Supervisory Board. The annual report contains the information on the total amount of payments made to the members of the Board of Directors and the members of the Supervisory Board.

- The Audit Committee does not consist mostly of independent Supervisory Board members. All the members of the Committee are Supervisory Board Members and two of them are an employees of the majority shareholder.

- The Company does not have a statement regarding bonus policies for the Board of Directors and the Supervisory Board. The Company publishes information on all payments to the members of the Board of Directors and the Supervisory Board. The said

information is published in aggregate within the Company's annual report.

- The Company carries out internal control through internal procedures which include the supervision of proper fulfilment of obligations. Therefore, within the meaning of the Code of Corporate Governance, there is no special organisational unit dealing exclusively with internal control.
- The Company published the amounts of remunerations paid to external auditors for the audit and other services.

Special Note:

The Supervisory Board has in place the Committee for the supervision of synergy measures, the Committee for appointments and bonuses (founded 10 December 2015), and at the beginning of 2016 the Audit Committee was founded with the purpose of a detailed analysis of financial reports, providing support to the Company's accounting and setting up a good and quality internal control of the Company.

## II. 1

### Internal Audit in the Company and Risk Management in Correlation with Financial Reporting

The Supervisory Board has set up an Audit Commission, with the task to analyze the financial reports in detail, support the Company's accounting and establish a good quality internal control of the Company.

The Company does not have a separate organizational unit tasked solely with internal auditing, but the Company does have a corporate security organizational unit that works on minimizing all operating risks, among its regular activities

## II. 2

### Significant Shareholders in the Company as per 31.12.2018.

As per 31.12.2018, the Company's majority shareholder is Zagrebačka banka d.d., having a 36.9% share in the share capital. It is followed by HT HOLDING with a 17.4% share in the share

capital. The biggest shareholder among physical persons is Marijan Hanžeković, holding a 3.17% share.

## II. 3

### Rules on Appointment and Recall of the members of the Board of Directors and the Supervisory Board and Their Powers

Pursuant to the Company Statute, Company's affairs are managed by a Board of Directors consisting of three to five members. One of the members is appointed as the Chairman of the Board. The Board of Directors is appointed and recalled by the Supervisory Board. The members of the Board of Directors are appointed for a term of 2 years and can be reappointed. Pursuant to the Companies Act and the Statute, the Board of Directors is solely responsible for conducting the Company's business and has the power to undertake all actions and make such decisions as it deems necessary for successful management of the

Company. The Board of Directors is obligated to observe the limitations set out in the Statute. Every member of the Board of Directors represents the Company jointly with another member of the Board of Directors.

The Supervisory Board consists of nine members, one of which is appointed by the employees. The General Meeting elects the Supervisory Board by an ordinary majority of votes, apart from the employee-appointed member. The mandate of Supervisory Board members is set at 4 years, and they can be re-elected. Supervisory Board members ele-

ct the Chairman and Deputy Chairman of the Supervisory Board amongst themselves. The Deputy Chair has the rights and obligations of the Chairman only when the Chairman is unable to carry out his/her function.

For specific transactions, or decisions of the Board of Directors, the Board of Directors is obligated to obtain the previous consent of the Supervisory Board, according to the criteria provided in Art. 15 of the Statute. Within its scope of activities, the Supervisory Board

handles the tasks laid down by Art. 18 of the Statute.

In line with Art. 8 of the Statute, within five years from the registration of Statute amendments with the Court Registry, the Board of Directors is authorized to increase the Company's share capital once or several times by a total sum of one hundred and eighty Croatian Kuna (authorized capital). Such a share capital increase requires the Supervisory Board's consent.

## Changes in the Company's Governing Bodies

II. 4

During 2018 there were changes in the Company's governing bodies.

The mandates of Zoran Kežman, the chairman of the Board of Directors, and Mirela Šešerko, member of the Board of Directors expired on 18 June 2018. In its meeting of 25 May 2018 the Supervisory Board appointed Boris Batelić as the Chairman of the Board of Directors.

The mandate of the newly elected chairman of the Board commenced on 19 June 2018 and is to go on for two years, pursuant to the Company's Statute.

The Supervisory Board reappointed the member of the Board of Directors, Mr. Tomislav Tadić. The mandate pursuant to the aforementioned Supervisory Board decision lasts two years and starts at the expiry of the current mandate, i.e. on 1 October 2018.

In light of the aforementioned changes, the Company Board of Directors consists of: Boris Batelić, Chairman of the Board of Directors, Irena Domjanović, member and Tomislav Tadić, member of the Board of Directors.

As per 1 May 2018 Marina Brajković and Maša Serdinšek resigned from their membership in the Supervisory Board, while the mandates of the former deputy chairperson Ariana Bazala-Mišetić and members Jasenka Anica Kreković, Marko Makek, Ana Hanžeković and Rozana Grgorinić expired on 18 June 2018.

On 14 June 2018 the General Meeting, among other decisions, rendered a decision on the election of new Supervisory Board Members, thus electing the following persons: Ariana Bazala-Mišetić, Ana Hanžeković, Rozana Grgorinić, Igor Radojković, Jelena Noveljić, Blaženka Klobas and Silvija Tadić. The mandate of the newly elected Supervisory Board members commenced on 19 June 2018 and is to go on for four years.

The newly elected Supervisory Board had a meeting on 19 June 2018, where they appointed Ariana Bazala-Mišetić as the deputy chairperson.

On 24 October 2018, the mandate of Ivica Hujek, the employee representative in the Supervisory Board expired.

In its meeting of 7 November 2018, the Workers' Council appointed Mrs. Suzana Čepl as a member of the Company's Supervisory Board, employee representative, with a four year mandate.

The Supervisory Board now works in the following structure: Igor Vavro, chairperson, Ariana Bazala-Mišetić, deputy chairperson, Ana Hanžeković, member, Rozana Grgorinić, member, Igor Radojković, member, Jelena Noveljić, member, Blaženka Klobas, member, Silvija Tadić, member, Suzana Čepl, employee representative.

The Company does not have a written diversity policy.

## Independent Auditor's Report on the Annual Report and Consolidated and Unconsolidated Financial Reports

III.