

TIGAR A.D., PIROT

**Consolidated Financial Statements
Year Ended December 31, 2011 and
Independent Auditors' Report**

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This is a translation of the original Auditors' Report issued in the Serbian language

INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Shareholders of TIGAR A.D., Pirot

We have audited the accompanying consolidated financial statements (pages 3 to 47) of Tigar A.D., Pirot (the "Company") and its subsidiaries (collectively: the "Group"), which comprise the consolidated balance sheet as at December 31, 2011, and the related consolidated income statement, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of the significant accounting policies and other explanatory notes.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation of these consolidated financial statements in accordance with the accounting regulations of the Republic of Serbia, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

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

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

Basis of Modified Opinion

As it is disclosed in Note 7 to the consolidated financial statements, the income from own work capitalized for the year ended December 31, 2011 totaled RSD 710,666 thousand and comprises:

- the effects of valuation of properties that the Parent Company transferred to its subsidiaries in the form of capital contribution increase of RSD 183,019 thousand, which the Group recorded in accordance with the Opinion of the Ministry of Finance (Note 2.1) whereby transfer of disposal rights over property from the parent company to its subsidiary within capital increase procedure, is in its substance transfer, i.e. retirement, which was then applied to the consolidated financial statements as well. The afore described treatment departs from the Group's accounting policy and requirements of IAS 16 "Property, Plant and Equipment," whereby the effects of increase in property value based on revaluation should be recorded within revaluation reserves and deferred tax liabilities, in the respective amounts of RSD 164,717 thousand and RSD 18,302 thousand.

(Continued)

This is a translation of the original Auditors' Report issued in the Serbian language

INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Shareholders of TIGAR A.D., Pirot

Basis of Modified Opinion (Continued)

- the costs of material and employee benefits capitalized and directly attributed to the property, plant and equipment under construction in order to improve business operations and reconstruct retail outlets and servicing network facilities in the amount of RSD 527,647 thousand. The Group's management holds the aforementioned investments are necessary for the purpose of improving business operations through the increase in sales volume, development of new products and reconstruction of retail stores and servicing and distribution network intended for direct sales to customers without intermediaries and aiming at the highest possible margin percentage, whereof the management expects economic benefits in the ensuing period. Based on the available documentation and audit procedures conducted, we could not satisfy ourselves as to whether the conditions for recognizing assets under construction were entirely fulfilled in accordance with requirements of IAS 16 "Property, Plant and Equipment." In addition, for intangible assets and property, plant and equipment under construction in respective amounts of RSD 337,259 thousand (Note 19) and RSD 740,753 thousand (Note 20), the Group failed to perform testing, i.e. to check whether these investments had been impaired in accordance with requirements of IAS 36 "Impairment of Assets," and determine whether their recoverable amounts were below their carrying amounts. Accordingly, we were unable to assess potential effects of the aforescribed inconsistencies on the accompanying consolidated financial statements.

As disclosed in Note 23 to the consolidated financial statements, inventories of goods stated as of December 31, 2011 as totaling RSD 1,301,484 thousand include certain slow-moving inventories which, due to the nature of accounting records, we were unable to quantify. The Group's management did not make allowance for impairment of the inventories given that it believes that they will be realized in the ensuing periods with regard to specific market characteristics, features of the inventories and their long useful lives. Based on the documentation made available to us, we could not satisfy ourselves as to whether additional allowance for impairment of inventories was necessary, i.e. reduction of inventories to their net realizable value in accordance with requirements of IAS 2 "Inventories."

As it is disclosed in Note 31 to the consolidated financial statements, two Group's adequacy indicators were not in compliance with the terms of the relevant loan agreements as of December 31, 2011, which, among other issues, allows the creditor to request early loan repayment. Accordingly, the long-term borrowings stated at December 31, 2011 as totaling RSD 732,486 thousand should have been presented within short-term financial liabilities. The Group's management does not expect adverse effects thereof given the fact that the creditor did not deliver any payment reminders or requested early repayment from the loan approval date up to the date of this report issuance.

Modified Opinion

In our opinion, except for the possible effect of the matters described in the Basis of Modified Opinion paragraph, the consolidated financial statements of the Group for the year ended December 31, 2011 have been prepared, in all material respects, in accordance with the accounting regulations of the Republic of Serbia.

Emphasis of Matter

We draw attention to the fact that the accompanying consolidated financial statements have been prepared on a going concern assumption. As disclosed in Note 2.5 to the consolidated financial statements, the Group incurred loss for the year ended December 31, 2011 in the amount of RSD 309,133 thousand, whereas the Group's current liabilities exceeded its current assets by RSD 778,021 thousand as of the same date. In addition, in 2011, all cash outflows from operating activities exceeded cash inflows by RSD 694,523 thousand. These matters, together with matters described in the Basis of Modified Opinion paragraph, suggest materially significant uncertainties that may cast substantial doubt upon the Group's ability to continue as a going concern. The consolidated financial statements do not include adjustments that may arise from the aforementioned uncertainties. In order to overcome those uncertainties, the Group's management has taken measures disclosed in Note 2.5. Our opinion is not modified in respect of these matters.

Belgrade, May 18, 2012

Zoran Nešić,
Certified Auditor

CONSOLIDATED INCOME STATEMENT
Year Ended December 31, 2011
(thousands of RSD)

	Notes	2011	2010
OPERATING INCOME			
Sales of goods, products and services	5	4,296,923	4,288,191
Own work capitalized	7	710,666	743,239
Increase in inventories		264,350	89,828
Other operating income	8	<u>26,546</u>	<u>39,624</u>
		5,298,485	5,160,882
OPERATING EXPENSES			
Cost of commercial goods sold		(836,916)	(902,193)
Cost of materials	9	(1,862,687)	(1,563,187)
Staff costs	10	(1,770,138)	(1,611,720)
Depreciation, amortization and provisions	11	(177,188)	(187,982)
Other operating expenses	12	<u>(638,622)</u>	<u>(624,515)</u>
		(5,285,552)	(4,889,597)
PROFIT FROM OPERATIONS		<u>12,934</u>	<u>271,285</u>
Finance income	13	108,672	72,209
Finance expenses	14	(537,174)	(391,035)
Other income	15	237,660	74,505
Other expenses	16	<u>(57,822)</u>	<u>(46,648)</u>
LOSS BEFORE TAXATION		<u>(235,731)</u>	<u>(19,684)</u>
Income taxes			
- Current income tax expense	17	(65,456)	(31,088)
- Deferred income tax expense		<u>(7,946)</u>	<u>(6,349)</u>
LOSS FOR THE YEAR		<u>(309,133)</u>	<u>(57,121)</u>
Net (loss) / profit attributable to:			
- majority shareholders		(326,650)	(62,560)
- non-controlling (minority) interest		<u>17,519</u>	<u>5,439</u>
Earnings per share (in RSD)		<u>(179.89)</u>	<u>(33.24)</u>

The accompanying notes on the following pages
are an integral part of these consolidated financial statements.

These consolidated financial statements were approved on April 30, 2012 by the management of Tigar A.D.,
Pilot.

Signed on behalf of Tigar A.D., Pilot by:

Dragan Nikolić
General Manager

Aleksandra Lilić
Preparer of Financial Statements

CONSOLIDATED BALANCE SHEET
As of December 31, 2011
(thousands of RSD)

	Notes	2011	2010
ASSETS			
Non-current assets			
Intangible assets	19	547,151	398,125
Property, plant and equipment	20	4,521,484	4,288,114
Investment property	20	227,011	-
Equity investments	21	11,819	11,819
Other long-term financial placements	22	41,720	45,468
		<u>5,349,185</u>	<u>4,743,526</u>
Current assets			
Inventories	23	2,073,287	1,823,646
Assets held-for-sale	24	6,846	20,039
Accounts receivable	25	892,958	903,162
Receivables for prepaid income taxes		2,171	7,097
Short-term financial placements		4,765	4,986
Cash and cash equivalents	26	251,093	369,524
Value added tax and prepayments	28	301,178	327,267
		<u>3,532,298</u>	<u>3,455,721</u>
Deferred tax assets	17	22,160	21,305
Total assets		<u><u>8,903,643</u></u>	<u><u>8,220,552</u></u>
EQUITY AND LIABILITIES			
Equity and reserves			
Share capital	29	2,062,152	2,062,152
Reserves		5,418	941
Revaluation reserves		1,079,077	1,051,401
(Accumulated losses) / retained earnings		(167,411)	197,134
Translation reserves		44,198	26,868
Capital attributable to majority shareholders		3,023,434	3,338,496
Non-controlling (minority) interest		72,688	55,169
		<u>3,096,122</u>	<u>3,393,665</u>
Long-term provisions and liabilities			
Long-term provisions	30	84,127	83,087
Long-term liabilities	31	1,270,109	1,729,282
		<u>1,354,236</u>	<u>1,812,369</u>
Current liabilities			
Short-term financial liabilities	32	2,684,202	1,716,210
Accounts payable	33	1,164,507	851,145
Other current liabilities	34	296,432	183,926
Value added tax and other public duties payable and accruals	35	114,852	110,455
Income taxes payable		50,326	18,086
		<u>4,310,319</u>	<u>2,879,822</u>
Deferred tax liabilities	17	142,966	134,696
Total equity and liability		<u><u>8,903,643</u></u>	<u><u>8,220,552</u></u>

The accompanying notes on the following pages are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
Year Ended December 31, 2011
(thousands of RSD)

	Share Capital	Reserves	Revaluation Reserves	(Accumulated Loss)/ Retained Earnings	Translation Reserves	Capital Attributable to Majority Shareholders	Non- Controlling Interest	Total
Balance January 1, 2010	2,062,152	207,925	1,074,215	85,934	34,127	3,464,353	49,730	3,514,083
Dividends paid to shareholders	-	-	-	(37,894)	-	(37,894)	-	(37,894)
Transfer	-	(206,215)	-	206,215	-	-	-	-
Effects of foreign currency fluctuations	-	-	-	-	(7,259)	(7,259)	-	(7,259)
(Loss)/profit for the year	-	-	-	(62,560)	-	(62,560)	5,439	(57,121)
Other	-	(769)	(22,814)	5,439	-	(18,144)	-	(18,144)
Balance, December 31, 2010	<u>2,062,152</u>	<u>941</u>	<u>1,051,401</u>	<u>197,134</u>	<u>26,868</u>	<u>3,338,496</u>	<u>55,169</u>	<u>3,393,665</u>
Balance January 1, 2011	2,062,152	941	1,051,401	197,134	26,868	3,338,496	55,169	3,393,665
Revaluation effects	-	-	69,211	-	-	69,211	-	69,211
Dividends paid to shareholders	-	-	-	(37,895)	-	(37,895)	-	(37,895)
Sales of property and equipment	-	-	(29,875)	-	-	(29,875)	-	(29,875)
Effects of foreign currency fluctuations	-	-	-	-	17,330	17,330	-	17,330
(Loss)/profit for the year	-	-	-	(326,650)	-	(326,650)	17,519	(309,131)
Other	-	4,477	(11,660)	-	-	(7,183)	-	(7,183)
Balance, December 31, 2011	<u>2,062,152</u>	<u>5,418</u>	<u>1,079,077</u>	<u>(167,411)</u>	<u>44,198</u>	<u>3,023,434</u>	<u>72,688</u>	<u>3,096,122</u>

The accompanying notes on the following pages
are an integral part of these consolidated financial statements.

CONSOLIDATED CASH FLOW STATEMENT
Year Ended December 31, 2011
(thousands of RSD)

	<u>2011</u>	<u>2010</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash receipts from customers	4,282,666	4,216,087
Interest receipts	83	3,877
Other receipts from operating activities	238,940	61,589
Cash paid to suppliers	(2,894,920)	(3,066,000)
Gross salaries and other staff costs paid	(1,719,868)	(1,624,709)
Interest paid	(399,169)	(256,169)
Income taxes payable	(14,991)	(21,235)
Other public duties payable	(187,264)	(186,118)
<i>Net cash used in operating activities</i>	<u>(694,523)</u>	<u>(872,678)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Sale of property, plant and equipment	114,253	17,986
Interest received and other placements	8,375	8,507
Dividends received	-	72
Purchases of property, plant and equipment	(48,288)	(177,269)
<i>Net cash provided by/ (used in) investing activities</i>	<u>74,330</u>	<u>(150,704)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Long-term and short-term loans (net inflows)	486,418	466,040
Other long-term and short-term liabilities	46,529	243,763
Finance lease payments	(21,256)	(15,129)
Dividends paid	-	(34,083)
<i>Net cash provided by financing activities</i>	<u>511,691</u>	<u>660,591</u>
NET CASH INCREASE	-	-
NET CASH DECREASE	(108,502)	(362,791)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	369,524	702,009
Foreign exchange (losses) / gains on translation of cash and cash equivalents, net	<u>(9,929)</u>	<u>30,306</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>251,093</u>	<u>369,524</u>

The accompanying notes on the following pages are an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***1. GENERAL INFORMATION ON THE COMPANY AND THE GROUP**

Tigar A.D., Pirot (the "Company" OR THE "Parent Company") was founded in 1935 through the establishment of an industrial workshop engaged in the production of a variety of rubber products and rubber-constructed shoes. After a temporary cessation of its business activities during World War II, the Factory resumed its operations on December 20, 1945. In 1972, the Company was the first in the former Yugoslavia to introduce, by its own technological and construction processes, the production of radial automobile tires manufactured with an inner textile belt. During 1991 the Company changed its legal form from that of a socially-owned enterprise to a shareholding company operating under mixed ownership, and on July 16, 1996, the Company changed its name to Tigar, the shareholding company doing business in the manufacture of rubber products (Tigar A.D., Pirot).

As of January 1, 2003 the Company underwent legal reorganization and status changes, whereby its organizational units, Fabrika Autoguma (tire production factory) and Fabrika unutrašnjih guma (inner tube production factory) separated from the Company and joined the newly-established entity, Tigar M.H., a Company for the Production of Tires, D.O.O., Pirot ("TMH") in which the Company held an equity interest of 65%. During 2005, the minority investors of Tigar MH made additional capital contributions, whereby the Company's equity interest changed from 65% to 50%. In accordance with the relevant partners' agreement, the registered share of the Company in Tigar MH with the Company Register is 49.4%. Taking into account the date of registration and the date of additional capital contributions paid by minority investors, the Company's investment in Tigar MH for 2005, calculated on a "pro-rata temporis" basis is 51.7674% and 51.9033%, respectively. During 2007, the Company's 19.4% equity investment in "Tigar Tyres" (previously known as "Tigar MH") was sold to the entity Michelin, Netherlands. As of December 31, 2007, based on the registration, the Company's investments in "Tigar Tyres" (previously known as: "Tigar MH"), amounted to 30%.

In 2008, the Company sold another 10% of its equity interest to Michelin, Netherlands. Thus, at December 31, 2008, equity interest in Tigar Tyres amounted to 20%. In 2009, the Company sold the remaining 20% of equity in this entity. Accordingly, the entity "Tigar Tyres," Pirot was not included in the consolidated financial statements of the Company prepared at December 31, 2009 and 2008.

In addition, based on the Board of Directors' Resolution dated December 16, 2002, subsequent to the legal separation of its former organizational units, eight newly-formed entities, all wholly-owned by the Company, were registered with the Commercial Court of Niš on December 26 and 27, 2002. These entities commenced their business activities on January 1, 2003. From April 1, 2005, subsequent to its separation from the Company, the newly-formed, wholly-owned entity, Tigar Trgovine D.O.O., Pirot (Trading entity), commenced its business operations.

In addition to the production of rubber products, the Company's principal activities also include the production of glues and utensils, transport, construction services, tourism and accommodation, foreign trade operations related to the activity for which the Company was established, special forms of foreign trade (agreements on long-term production cooperation, compensation transactions, purchase of goods abroad for the purpose of resale abroad, as well as export of purchased and imported goods), services in foreign trade and the like.

The Company's governing administrative bodies are its Shareholders' Assembly, Board of Directors, Director and Supervisory Board.

The Company's registered office is located at the street address of Nikole Pašića 213, in Pirot.

As of December 31, 2011, the Company had 485 employees (December 31, 2010: 476 employees) whereas the Group had 2,024 employees altogether (December 31, 2010: 2,026 employees).

The tax identification number of the Company is 100358298 and its company registration number is 07187769.

In accordance with the Decision of the Securities Commission governing the listings and quotations on the Belgrade Stock Exchange (BELEX), enacted on April 2, 2007, the Company's shares were admitted to the A listing of BELEX. These are common voting shares. The symbol – TIGR. Trading method – continuous trading method.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

*All amounts are expressed in thousands of RSD, unless otherwise stated.***2. BASIS OF PREPARATION AND PRESENTATION OF THE CONSOLIDATED FINANCIAL STATEMENTS****2.1. Basis for Consolidation**

The accompanying financial statements represent the consolidated financial statement of the Company Tigar A.D., Pirot (the "Company" or "Parent Company"), and the financial statements of the following subsidiaries (collectively: the "Group")

	% Equity Interest
1 Tigar Obuća d.o.o., Pirot	100.00%
2 Tigar Hemijski proizvodi d.o.o., Pirot	100.00%
3 Tigar Tehnička guma d.o.o., Pirot	100.00%
4 Tigar Trejd d.o.o., Pirot	100.00%
5 Tigar Poslovni servis d.o.o., Pirot	100.00%
6 Tigar Tours d.o.o., Pirot	100.00%
7 Tigar Obezbeđenje d.o.o., Pirot	100.00%
8 Tigar Zaštitna radionica d.o.o., Pirot	100.00%
9 Tigar Inter Risk d.o.o., Pirot	100.00%
10 Tigar Inkon d.o.o., Pirot	100.00%
11 Slobodna Zona Pirot A.D., Pirot	75.06%
12 Tigar Montenegro d.o.o., Podgorica, Montenegro	80.00%
13 Tigar Patner d.o.o., Skopje, Republic of Macedonia	70.00%
14 D.O.O. Tigar Trejd, Banja Luka, Republic of Srpska	70.00%
15 Tigar Americas Jacksonville, Florida, USA	100.00%
16 Tigar Europe, London, UK	50.00%

The financial statements of foreign subsidiaries stated in their functional currencies are translated into the reporting currency of the Parent Company (Dinar), by translating the assets and liabilities at the official exchange rate as of the balance sheet date, and by translating income and expenses at the average rates of exchange prevailing during the year.

All material intercompany balances and transactions relating to the abovelisted subsidiaries have been eliminated upon consolidation.

2.2. Basis of Preparation and Presentation of Consolidated Financial Statements

Pursuant to the Law on Accounting and Auditing (Official Gazette of the Republic of Serbia no. 46 of June 2, 2006 and no. 111 as of December 29, 2009), legal entities and entrepreneurs incorporated in Serbia are required to maintain their books of account, to recognize and value assets and liabilities, income and expenses, and to present, submit and disclose financial statements in conformity with the prevailing legislation and professional rules which include: the Framework for the Preparation and Presentation of Financial Statements (the "Framework"), International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS), as well as the related interpretations representing an integral part of these standards which were in effect as at December 31, 2002.

The amendments to IAS, as well as the newly-issued IFRS and the related interpretations issued by the International Accounting Standards Board ("IASB") and the International Financial Reporting Interpretations Committee ("IFRIC"), in the period between December 31, 2002 and January 1, 2009, were officially adopted pursuant to a Decision enacted by the Ministry of Finance of the Republic of Serbia ("Ministry") and published in the Official Gazette of the Republic of Serbia number 77 of October 25, 2010.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***2. BASIS OF PREPARATION AND PRESENTATION OF THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)****2.2. Basis of Preparation and Presentation of Consolidated Financial Statements (Continued)**

However, until the preparation date of the accompanying consolidated financial statements, not all amendments to IAS/IFRS and IFRIC in effect for annual periods beginning on or after January 1, 2009 had been translated. In addition, the accompanying consolidated financial statements are presented in the format prescribed under the "Guidelines on the Prescribed Form and Content of the Financial Statements of Enterprises, Cooperatives and Entrepreneurial Ventures" (Official Gazette of the Republic of Serbia, nos. 114/2006 to 3/2011). Such statements represent the complete set of financial statements as defined under the law, which differ from those defined under the provisions of IAS 1, "Presentation of Financial Statements," and differ in some respects, from the presentation of certain amounts as required under the aforementioned standard. Standards and interpretations in issue, but not yet officially translated and adopted and standards and interpretations in issue but not yet in effect are disclosed in Notes 2.3 and 2.4.

In addition to the aforementioned, the accounting regulations of the Republic of Serbia depart from IFRS in the following respects:

- Pursuant to the Opinion of the Ministry issued on January 22, 2009, transfer of rights of handling and using property from a parent company to its subsidiary, as a means of increasing capital, has the character of transfer and/or disposal. Also, according to the aforementioned Ministry's opinion, the difference between the appraised value of property, based on which the value of additional equity stake of the parent company is determined, and its carrying value included the business books of the parent, is credited to income of the period. The aforementioned accounting treatment is a departure from IAS 16 "Property, Plant and Equipment," which requires that: 1) the revaluation result be attributed directly to equity to the position of revaluation reserves, i.e. that it be recognized within income presented in the income statement up to the amount of reversal of revaluation reserves accumulated for that asset and previously recognized within expenses; also 2) revaluation reserves which are a component part of equity relating to property, plant and equipment may be transferred directly to retained earnings, once the asset is derecognized. In addition, income recognition applied in the accompanying financial statements that is in accordance with the aforementioned opinion, departs from the requirements of IAS 18 "Revenues."
- As in accordance with the Rules on Amendments and Supplements to the Rules on the Chart of Account for Companies, Cooperatives, Other Legal Entities and Entrepreneurs which came in effect as of January 24, 2011, in preparing the annual consolidated financial statements as of and for the year ended December 31, 2010, legal entities and entrepreneurs may decide not to disclose the net effects of foreign currency clause related to receivables and payables denominated in foreign currency within income and expenses of the current period. In the aforementioned case, net effect of the contractually agreed currency clauses is stated within other prepayments/accruals (Notes 3.3 and 25). The proportionate amount of deferred currency clause effects is transferred to the accounts of foreign exchange losses and gains as of the date upon which the respective payable if due for settlement and receivable is due for collection. The Company exercised this option in the preparation of 2010 and 2009 consolidated financial statements. The aforementioned accounting treatment departs from the provisions IAS 21 "Effects of Changes in Foreign Exchange Rates."

In accordance with the aforescribed, and given the potentially material effects which the departures of accounting regulations of the Republic of Serbia from IAS and IFRS may have on the fairness presentations made in the consolidated financial statements, the accompanying consolidated financial statements cannot be treated as a set of consolidated financial statements prepared in accordance with IAS and IFRS.

The consolidated financial statements were prepared at historical cost principle, unless otherwise stipulated in the accounting policies presented hereunder.

In the preparation of the accompanying consolidated financial statements, the Group adhered to the accounting policies described in Note 3.

The Group's consolidated financial statements are stated in thousands of dinars (RSD). The dinar is the official reporting currency in the Republic of Serbia.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***2. BASIS OF PREPARATION AND PRESENTATION OF THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)****2.3. Standards and Interpretations in Issue, but not yet Translated and Adopted**

As of the consolidated financial statements issuance date, the following standards, amendments were issued by the International Accounting Standards Board and Interpretations issued by the International Financial Reporting Interpretations Committee but were not officially adopted and translated in the Republic of Serbia for the annual accounting periods commencing on or after January 1, 2010:

- Amendments to IFRS 7 “Financial Instruments: Disclosures” – Amendments improving fair value and liquidity risk disclosures (revised in March 2009, effective for annual periods beginning on or after January 1, 2009);
- Amendments to IFRS 1 “First-time Adoption of IFRS” – Additional Exemptions for First-time Adopters. The amendments relate to assets in oil and gas industry and determining whether an arrangement contains a lease (revised in July 2009, effective for annual periods beginning on or after January 1, 2010);
- Amendments to various standards and interpretations resulting from the Annual quality improvement project of IFRS published on April 16, 2009 (IFRS 5, IFRS 8, IAS 1, IAS 7, IAS 17, IAS 36, IAS 39, IFRIC 16) primarily with a view to removing inconsistencies and clarifying wording, (amendments are to be applied for annual periods beginning on or after 1 January 2010, while the amendment to IFRIC is to become effective as of July 1, 2009);
- Amendments to IAS 38 “Intangible Assets” (revised in July 2009, effective for annual periods beginning on or after July 1, 2009);
- Amendments to IFRS 2 “Share-based Payment”: Amendments resulting from the Annual quality improvement project of IFRS (revised in April 2009, effective for annual periods beginning on or after July 1, 2009) and amendments relating to group cash-settled share-based payment transactions (revised in June 2009, effective for annual periods beginning on or after January 1, 2010);
- Amendments IFRIC 9 “Reassessment of Embedded Derivatives” effective for annual periods beginning on or after July 1, 2009 and IAS 39 “Financial Instruments: Recognition and Measurement” – Embedded Derivatives (effective for annual periods beginning on or after June 30, 2009);
- IFRIC 18 “Transfers of Assets from Customers” (effective for annual periods beginning on or after July 1, 2009);
- “Conceptual Framework for Financial Reporting 2010” being an amendments to “Framework for the Preparation and Presentation of Financial Statements” (effective for transfer of assets from customers received on or after September 2010);
- Amendments to IFRS 1 “First-time Adoption of International Financial Reporting Standards” – Limited Exemption from Comparative IFRS 7 Disclosures for First-time Adopters (effective for annual periods beginning on or after July 1, 2010);
- Amendments to IAS 24 “Related Party Disclosures” – Simplifying the disclosure requirements for government-related entities and clarifying the definition of a related party (effective for annual periods beginning on or after January 1, 2011);
- Amendments to IAS 32 “Financial Instruments: Presentation” – Accounting for rights issues (effective for annual periods beginning on or after February 1, 2010);
- Amendments to various standards and interpretations “Improvements to IFRSs” resulting from the Annual quality improvement project of IFRS published on May 6, 2010 (IFRS 1, IFRS 3, IFRS 7, IAS 1, IAS 27, IAS 34, IFRIC 13) primarily with a view to removing inconsistencies and clarifying wording, (most amendments are to be applied for annual periods beginning on or after January 1, 2011);

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***2. BASIS OF PREPARATION AND PRESENTATION OF THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)****2.3. Standards and Interpretations in Issue, but not yet Translated and Adopted (Continued)**

- Amendments to IFRIC 14 "IAS 19 – The Limit on a defined benefit Asset, Minimum Funding Requirements and their Interaction" – Prepayments of a Minimum Funding Requirement (effective for annual periods beginning on or after January 1, 2011);
- IFRIC 19 "Extinguishing Financial Liabilities with Equity Instruments" (effective for annual periods beginning on or after July 1, 2010).

2.4. Standards and Interpretations in Issue not yet in Effect

At the date of issuance of these consolidated financial statements the following standards, revisions and interpretations were in issue but not yet effective:

- IFRS 9 "Financial Instruments" (effective for annual periods beginning on or after January 1, 2015);
- IFRS 10 "Consolidated Financial Statements" (effective for annual periods beginning on or after January 1, 2013);
- IFRS 11 "Joint Arrangements" (effective for annual periods beginning on or after January 1, 2013);
- IFRS 12 "Disclosures of Involvement with Other Entities" (effective for annual periods beginning on or after January 1, 2013);
- IFRS 13 "Fair Value Measurement" (effective for annual periods beginning on or after January 1, 2013);
- IAS 27 (revised in 2011) "Separate Financial Statements" (effective for annual periods beginning on or after January 1, 2013);
- IAS 28 (revised in 2011) "Investments in Associates and Joint Ventures" (effective for annual periods beginning on or after January 1, 2013);
- Amendments to IFRS 1 "First-time Adoption of IFRS" – Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters (effective for annual periods beginning on or after July 1, 2011);
- Amendments to IFRS 7 "Financial Instruments: Disclosures" – Transfers of Financial Assets (effective for annual periods beginning on or after January 1, 2011);
- Amendments to IFRS 7 "Financial Instruments: Disclosures" – Offsetting Financial Assets and Financial Liabilities (effective for annual periods beginning on or after January 1, 2013);
- Amendments to IFRS 9 "Financial Instruments" and IFRS 7 "Financial Instruments: Disclosures" – Mandatory Effective Date and Transition Disclosures;
- Amendments to IAS 1 "Presentation of Financial Statements" – Presentation of Items of Other Comprehensive Income (effective for annual periods beginning on or after July 1, 2012);
- Amendments to IAS 12 "Income Taxes" – Deferred Tax: Recovery of Underlying Assets (effective for annual periods beginning on or after January 1, 2012);
- Amendments to IAS 19 "Employee Benefits" – Improvements to the Accounting for Post-employment Benefits (effective for annual periods beginning on or after January 1, 2013);
- Amendments to IAS 32 "Financial Instruments: Presentation" – Offsetting Financial Assets and Financial Liabilities (effective for annual periods beginning on or after January 1, 2014);
- IFRIC 20 "Stripping Costs in the Production Phase of a Surface Mine" (effective for annual periods beginning on or after January 1, 2013).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***2. BASIS OF PREPARATION AND PRESENTATION OF THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)****2.5. Going Concern**

The Group incurred loss for the year ended December 31, 2011 in the amount of RSD 309,133 thousand, whereas the Group's current liabilities exceeded its current assets by RSD 778,021 thousand as of the same date. In addition, in 2011, all cash outflows from operating activities exceeded cash inflows by RSD 694,523 thousand.

In the previous period, the Group's business operations were affected by the economic crisis and deteriorating conditions. In 2012, the Group expects better conditions in the economy; however, due to the current global market crisis and its impact on the Serbian market, the Group expects to continue its business operations in difficult and uncertain circumstances. The impact of the crisis on the Group's operations is not entirely predictable, therefore, there is an element of general uncertainty. In prior years, as well as in 2011, the Group made considerable effort to define and reschedule major Group's debts (Note 31), and significant amounts were invested in new production capacities and new product development.

The Group's management expects to be able to convert current liabilities into long-term liabilities, upon the creditor's consent, as well as to obtain new sources of long-term financing in order to settle the commitments. In addition, the management hopes that the creditors may decide to convert portion of long-term liabilities into equity or additionally increase capital contributions in subsidiaries in the ensuing period.

In addition to the aforescribed plans to overcome the liquidity issues and stabilize regular operations, the Groups' management expects that the conducted reorganization and centralization of the distribution function with regard to extending range of sales of services, significant investments in new production capacities and retail and servicing networks and increased production volume in subsidiaries as well as favorable conditions in the footwear and technical rubber markets will have positive effects on the Group's business operations in the subsequent periods.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**3.1. Revenue and Expense Recognition and Measurement**

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods sold and services provided throughout the normal course of business, net of discounts, value added taxes and other sales taxes.

Income from sales of products and goods is recognized when the risk and rewards associated with the right of ownership are transferred to the customer; which is considered to be the date upon which products are delivered to the customer.

At the time when income is recognized, the related expenditure is also recognized (as per the "matching principle").

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)****3.2. Borrowing Costs**

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale. A qualifying asset is an asset that takes a substantial period of time to get ready for its intended use or sale.

Investment income realized from the temporary placement of funds borrowed is netted against borrowing costs intended to finance qualifying assets.

All other borrowing costs are recognized on the profit and loss account in the period to which these relate.

3.3. Foreign Exchange Translation

Transactions denominated in foreign currencies are translated into dinars at the official exchange rates in effect at the date of each transaction.

Assets and liabilities denominated in foreign currencies are translated into dinars by applying the official exchange rates prevailing at the balance sheet date, unless loan of finance lease agreement stipulate otherwise.

Foreign exchange gains or losses arising upon the translation of transactions, and assets and liabilities in foreign currencies are credited or charged to the income statement, except for the effects of currency clause indexed to long-term receivables and payables denominated in dinars, which are presented on the line item of other accruals or other prepayments. The proportionate amount of deferred foreign currency clause effects is transferred to the accounts of foreign currency clause gains and losses at the date when the liability falls due for settlement or a receivable becomes due for collection.

3.4. Employee Benefits*a) Taxes and Contributions Made to the Employee Social Security and Insurance Funds*

In accordance with regulatory requirements, the Group is obligated to pay contributions to tax authorities and to various state social security funds that guarantee social security insurance benefits to employees. These obligations involve the payment of taxes and contributions on behalf of the employee, by the employer, in an amount computed by applying the specific, legally-prescribed rates. The Group is also legally obligated to withhold contributions from gross salaries to employees, and on behalf of its employees, to transfer the withheld portions directly to the applicable government funds. These taxes and contributions payable on behalf of the employee and employer are charged to expenses in the period in which they arise.

b) Obligations for Retirement Benefits and Jubilee Awards

The Group is under obligation to pay to its employees retirement benefits, depending on the years of service with the Group in the amount of three salaries which the employee earned in the month preceding the payment, i.e., in the amount of an average salary in the Group in the month preceding the payment of retirement benefit, if such arrangement proves more favorable for the employee.

In addition, the Group is under obligation to pay jubilee awards for 20 and 30 years of service with the Group and upon his/her retirement, payable in gold coins of 3, 6 and 9 grams of gold.

The Group formed provisions for the liabilities based on the aforementioned and adequate disclosures are included in Note 30.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)****3.5. Taxes and Contributions***a) Current Income Tax*

Current income tax represents the amount calculated in accordance with the Income Tax Law effective in the Republic of Serbia. The annual corporate income tax is payable at the rate of 10% on the tax base reported in the annual income tax return, as reduced by any applicable tax credits. The taxable base includes the profit stated in the statutory statement of income, as adjusted for permanent differences that are specifically defined under local tax rules.

The effective tax regulations in the Republic of Serbia do not allow any tax losses of the current period to be used to recover taxes paid within a specific carryback period. However, any current year losses may be used to reduce or eliminate taxes to be paid in future periods for a duration of no longer than five ensuing years. Tax losses incurred prior to January 1, 2010 are available for carryforward and may be utilized against future profits for a period of ten years.

b) Deferred Income Taxes

Deferred income tax is determined using the balance sheet liability method, for temporary differences arising between the tax bases of assets and liabilities components, and their carrying values in the consolidated financial statements. The currently-enacted tax rates at the balance sheet date are used to determine the deferred income tax amount. Deferred tax liabilities are recognized for all taxable temporary differences. Deferred tax assets are recognized for deductible temporary differences, and the tax effects of income tax losses and credits available for carry forward, to the extent that it is probable that future taxable profit will be available against which deferred tax assets may be utilized.

c) Indirect Taxes and Contributions

Indirect taxes and contributions include property taxes and other taxes and contributions include property taxes, taxes and contributions paid by employer to or on behalf of employees, as well as other taxes and contributions paid pursuant to republic and municipal regulations, presented within Other operating expenses.

3.6. Intangible Assets

Intangible assets are stated in the Group's books of account at cost, as adjusted for accumulated amortization and any impairment losses.

Intangible assets comprise the capitalized cost of software, licenses and similar rights acquired through purchases, which are amortized over a period of five years.

In addition, intangible assets include internally-generated intangible assets mostly relating to the investments in development of projects the Group's management deems as necessary for the purpose of improving business operations via increase in sales volume, development of new products and reconstruction of retail stores and investments in developing servicing and distribution network to allow direct sales to customers without intermediaries in order to achieve the highest margin percentages possible, whereof the management expects economic benefits in the ensuing years.

Cost (cost price) of the separately acquired intangible assets is comprised of cost including customs duties and non-refundable turnover taxes payable, less any discounts and rebates or any costs directly attributable to bringing the asset into the condition necessary for its intended use.

Directly attributable costs are:

- Costs of employee benefits (defined by IAS 19) incurred directly during the process of preparing the asset in to the functional state;
- Professional service incurred directly during the process of preparing the asset in to the functional state; and
- Costs of testing functionality of the assets.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)****3.6. Intangible Assets (Continued)**

Recognition of expenses included within the carrying value of intangible assets ceases when the assets have been brought to the functional condition for the use intended by the managements. Therefore, the expenditure incurred during the usage or reallocation of intangible assets is not included in the carrying value of those assets.

An internally-generated intangible asset arising from development (or from the development phase of an internal project) is recognized as an asset and development activities refer to the following

- design, construction and testing of proto-types and models prior to production and usage;
- design of tools, assembled devices, molds and matrices relying on new technology;
- design, construction and testing of the selected alternatives to new or improved materials, devices, products, processes, systems or services.

The value of intangible assets with a limited useful life that is being amortized is systematically allocated during their useful life. The calculation of amortization commences when the assets are available for usage, i.e. when they are situated at the location and in condition ready for operation in the manner intended by the management.

Amortization of intangible assets ceases at the earlier of the date of classification as assets held for sale (or the date of their inclusion in the asset group intended for retirement classified as group of assets held for sale) in accordance with IFRS 5 and the date of derecognition.

The amortization method applied reflects the pattern of expected Company's consumption of the future benefits from the assets. In case the pattern cannot be reliably determined, amortization is provided using the straight-line method.

3.7. Property, Plant and Equipment

The items of plant, property and equipment qualifying for recognition, are initially stated at cost.

Cost represents the prices billed by suppliers together with all costs incurred in bringing new fixed assets into use, net of discounts.

Subsequent expenditures such as modification or adaptation to the assets is recognized as an increase in cost of the respective assets, when it is probable that future economic benefits, in excess of the originally assessed standard of performance, will flow to the Company, and when the cost can reliably be measured. All other subsequent expenditures are expensed as incurred.

If an asset's carrying amount is increased as a result of a revaluation, the increase is recognized in equity under the heading of revaluation surplus. However, the increase shall be recognized in profit or loss to the extent that it reverses a revaluation decrease of the same asset previously recognized in profit or loss, in which case the revaluation surplus is credited to income statement up to the amount in which the previously recognizes decrease was recorded within expenses.

If an asset's carrying amount is decreased as a result of a revaluation, the decrease is recognized in profit or loss. However, the decrease is recognized in other comprehensive income to the extent of any credit balance existing in the revaluation surplus in respect of that asset.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)****3.7. Property, Plant and Equipment (Continued)**

In 2011 and 2010, the Parent Company appraised the value of buildings transferred to subsidiaries as contribution in kind. The effects of appraising buildings that were not subject to valuation in prior years are credited to profit of the period.

Subsequent expenditures such as modification or adaptation to the assets is recognized as an increase in cost of the respective assets, when it is probable that future economic benefits, in excess of the originally assessed standard of performance, will flow to the Group, and when the cost can reliably be measured. All other subsequent expenditure is expensed as incurred.

The depreciation of property, plant and equipment is computed on a straight-line basis for every, individual item of property, plant and equipment in order to fully write off the cost of assets over their estimated useful lives by applying the following depreciation rates:

	<u>%</u>
Buildings	1.3% - 5%
Equipment	
Power stations	10%
Production equipment	12.5% - 14.3%
Molds	50%
Vehicles	14.3%
Cars	15.5%
Laboratory and measurement equipment	16.6%
Office furniture	12.5%
Computers	20%

3.8. Investment Property

Investment properties are properties held to earn rentals or for capital appreciation or both rather than be used to render services or for administrative or regular sales purposes. Investment properties are measured initially at cost, including transaction costs. Subsequent to initial recognition, investment properties are measured at fair value. Gains and losses arising from changes in the fair value of investment properties are included in profit or loss in the period in which they arise.

3.9. Impairment of Tangible Assets

At each balance sheet date, the Group's management reviews the carrying amounts of the Group's tangible assets. If there is any indication that such assets have been impaired, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. If it is not possible to estimate the recoverable amount of the individual asset, the Group shall determine the recoverable amount of the cash-generating unit to which the asset belongs.

The recoverable amount of an asset or a cash-generating unit is the higher of its fair value less costs to sell and its value in use. For the purposes of estimating value in use, future cash flows are discounted to the net book value by applying the discount rate before taxation reflecting the present market value of the time value of money and risks inherent in the asset.

If the estimated recoverable amount of assets (or cash generating unit) is below their carrying value, the carrying amount of the asset (or cash generating unit) is reduced to its recoverable amount. An impairment loss is recognized as an expense of the current period under operating expenses, except in case of land and buildings that are not used as investment property which is stated at revalued amount in which case impairment loss is presented as a loss on revaluation of assets.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)****3.9. Impairment of Tangible Assets (Continued)**

Where an impairment loss subsequently reverses, the carrying amount of the asset (or cash generating unit) is increased to the revised estimate of its recoverable value. However, this is performed so that the increased carrying amount does not exceed the carrying value that would have been determined had no impairment loss been recognized for the asset (or cash generating unit) in prior years. A reversal of an impairment loss is recognized as income immediately, unless the respective asset is carried at a revalued amount, in which instance, the reversal of the impairment loss is treated as a revaluation increase.

At December 31, 2011, the Group's management did not perform any testing in order to determine whether there were any indications of impairment in the Group's tangible assets.

3.10. Leases

Leases are classified as finance leases whenever the terms of the lease substantially transfer all risks and rewards of ownership to the Group. All other leases are classified as operating leases.

The Group as a Lessor

Lease income from operating leases (rentals) is recognized in income on a straight-line basis over the lease term. Initial direct costs incurred by lessors in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognized on a straight line basis over the lease term.

The Group as a Lessee

Assets held under finance leases are initially recognized as the assets of the Group at the present value of the minimum lease payments, which is determined at the inception of the particular lease. The corresponding liability to the lessor is included in the balance sheet as a finance lease liability.

Lease payments are apportioned between finance expenses and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance expenses are recognized immediately in profit or loss, unless they are directly attributable to qualifying assets, in which case they are capitalized in accordance with the Group's general policy on borrowing costs (Note 3.2).

Lease payments under an operating lease are recognized as an expense on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.

In the event that lease incentives are received to enter into operating leases, such incentives are recognized as a liability. The aggregate benefit of incentives is recognized as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

3.11. Inventories

Inventories are primarily stated at the lower of cost and net realizable value. The cost comprises invoiced value, cost of transport and other related costs. The net realizable value is the price at which inventories can be realized throughout the normal course of business, after allowing for the costs of realization.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)****3.11. Inventories (Continued)**

The value of work in progress and finished products include all costs directly attributable to production, as well as production overheads.

Inventories in retail outlets are carried at retail prices. At the end of each accounting period, the carrying value is adjusted to cost by an apportionment of the related retail price calculated on an average basis, between the cost of goods sold and the inventories held.

Goods for sale at warehouses are valued during the year at their wholesale prices. At the end of each accounting period, the carrying value is adjusted to cost by an apportionment of the related selling margin calculated on an average basis, between the cost of goods sold and the inventories held.

Provisions charged to "Other expenses" are made where appropriate in order to reduce the value of inventories to management's best estimate of net realizable value. Inventories found to be damaged or of a substandard quality are written off.

3.12. Financial Instruments

Financial instruments are initially measured at fair value as increased by the transaction costs (except for financial assets and liabilities carried at fair value through profit and loss) which are directly attributable to the acquisition or issuance of a financial asset or financial liability.

Financial assets and financial liabilities are recognized in the Group's consolidated balance sheet on the date upon which the Group becomes counterparty to the contractual provisions of a specific financial instrument.

Financial assets cease to be recognized when the Group loses control of the contractual rights governing such instruments; which occurs when the rights of use of such instruments have been realized, expired, abandoned, and/or ceded. Financial liabilities cease to be recognized when the Group fulfills the obligations, or when the contractual repayment obligation has either been cancelled or has expired.

a) Long-Term Financial Placements

Long-term financial placements are comprised of equity investments in other legal entities and are stated at cost less allowances for impairment.

b) Other Long-term Financial Placements

Other long-term financial placements are comprised of receivables from employees for residential housing loans that have been extended with 20-year maturities, and have been stated at nominal value which represents the present value of the future cash flows discounted at a contractually-agreed interest rate. In the opinion of the management, the effects of non-application of IAS 39 "Financial Instruments: Recognition and Measurement" requiring that long-term receivables be carried at amortized value by using the effective interest rate method are immaterial for the financial statements taken as a whole.

c) Accounts Receivable

Accounts receivable are stated at their nominal values as reduced by appropriate allowances for estimated bad debts. An allowance for impairment is recognized and charged to the income statement against domestic and foreign accounts receivable balances that are more than 180 days past due. The uncollectible receivables are written off either on the basis of a court decision or settlement agreed between the parties involved, or otherwise, based upon a relevant resolution of the Group's Board of Directors. Allowance for impairment of receivables from related parties is not calculated.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)****3.12. Financial Instruments (Continued)***d) Cash and Cash Equivalents*

In the cash flow statement, cash and cash equivalents entail cash on hand as well as balances on bank accounts with commercial banks. Cash and cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Cash equivalents represent demand deposits with commercial banks approved for the period of 90 days.

e) Accounts Payable

Accounts payable are stated at their nominal values.

f) Borrowings

Borrowings are initially recognized at fair value net of transaction costs, whereafter they are stated at amortized cost applying the contractually-agreed interest rate which approximates effective interest rate, and penalties, if any.

g) Impairment of Financial Assets

At each balance sheet date, financial assets, except for assets carried at fair value through profit and loss, are assessed for impairment. Impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset.

For shares not listed on the market which are classified as available-for-sale, a significant or prolonged decline in the fair value of an investment in an equity instrument below its cost is also objective evidence of impairment.

For all other financial assets, including redeemable securities classified as available for sale and receivables arising from finance lease, objective evidence of impairment may include:

- significant financial difficulty of the issuer or obligor;
- a breach of contract, such as a default or delinquency in interest or principal payments;
- it becoming probable that the borrower will enter bankruptcy or other financial reorganization.

For certain categories of financial assets, such as accounts receivable, that have been individually assessed for impairment and found not to be individually impaired are included in a collective assessment of impairment. The objective evidence of collective impairment could include previous experience with collection, delinquency in collection, as well as changes in the national or local economic circumstances that correlate with defaults.

For financial assets stated at amortized cost, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate.

4. SUMMARY OF SIGNIFICANT ACCOUNTING ESTIMATES

The presentation of the consolidated financial statements requires the Company's i.e. Group's management to make best estimates and reasonable assumptions that influence the assets and liabilities amounts, as well as the disclosure of contingent liabilities and receivables as of the date of preparation of the consolidated financial statements, and the income and expenses arising during the accounting period. These estimations and assumptions are based on information available to us, as of the date of preparation of the consolidated financial statements. Actual results may vary from these estimates.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***4. SUMMARY OF SIGNIFICANT ACCOUNTING ESTIMATES (Continued)**

What follows are the key assumptions in respect of the future events and other sources of estimations, uncertainties as of the consolidated balance sheet date which represent risk from material adjustments to the amounts of consolidated balance sheet items in the following fiscal year.

4.1. Depreciation and Amortization Charge and Rates Applied

The calculation of depreciation and amortization, as well as depreciation and amortization rates are based on the economic useful life of property, equipment and intangible assets. Once a year, the Group assesses the economic useful life based on the current estimates.

4.2. Allowance for Impairment of Receivables

We calculated the allowance for impairment of doubtful receivables based on the estimated losses arising from customer's default. Our assessment is based on the aging analysis of accounts receivable, historical write-offs, customer creditworthiness and changes in the terms of sale, identified upon determining the adequacy of allowance for impairment of doubtful receivables. This includes the assumptions on the future customer behavior and the resultant future collections. The management assesses that allowance for impairment of receivables, in addition to the amounts already disclosed in the accompanying consolidated financial statements, is not necessary.

4.3. Allowance for Impairment of Inventories

We calculated allowance for impairment of inventories based on the estimated losses due to impossibility of sales or realization within the production process. Our estimates are based on the analyses of movements in inventories, historical write-offs, estimates of the movements in sales market, sales targets, changes in terms of sales and in estimates of useful lives and conditions of inventories when determining allowance for impairment. This includes the assumptions on the future customer behavior and the resultant future sales. The management assesses that additional allowance for impairment of inventories is not necessary.

4.4. Fair Value

The fair value of financial instruments for which an active market does not exist is determined by applying adequate valuation methods. The Group applies its professional judgment in the selection of adequate methods and assumptions.

It is a policy of the Group to disclose the fair value information of those components of assets and liabilities for which published or quoted market prices are readily available, and of those for which the fair value may be materially different than their recorded amounts. In the Republic of Serbia, sufficient market experience, stability and liquidity do not exist for the purchase and sale of receivables and other financial assets or liabilities, for which published market prices are presently not readily available. As a result of this, fair value cannot readily or reliably be determined in the absence of an active market. The Group's management assesses its overall risk exposure, and in instances in which it estimates that the value of assets stated in its books may not have been realized, it recognizes a provision. In the opinion of management, the reported carrying amounts are the most valid and useful reporting values under the present market conditions.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

5. SALES OF PRODUCTS, GOODS AND SERVICES

	Year Ended December 31,	
	2011	2010
Sale on domestic market		
Sales of products and services on domestic market	1,607,516	1,586,456
Sale of goods on domestic market	242,712	344,705
	<u>1,850,228</u>	<u>1,931,161</u>
Sale on foreign market		
Sales of products and services on foreign markets	1,528,986	1,356,230
Sale of goods on foreign markets	917,709	1,000,800
	<u>2,446,695</u>	<u>2,357,030</u>
	<u><u>4,296,923</u></u>	<u><u>4,288,191</u></u>

6. OPERATING AND GEOGRAPHICAL SEGMENTS

Products and Services within Operating Segments

For management needs, the Group is organized in six operating segments. These segments are the basis for the Group's segment reporting. Basic products and services of each of the segments are as follows:

Rubber products – the manufacture and sale of rubber products such as: tire treads, pipes and flaps designated for the automotive industry, rubber products for mining, sporting equipment and balls.

Chemical products – the production and sale of a range of chemical products, including colors, polishes and other related products, glues and gelatin.

Footwear – the production and sale of rubber-made shoes.

Trade - retail trade and wholesale of products from the production program of other segments, as well as marketing, distribution and sale of inner and outer car tires.

Services – providing services to tourist agencies, hotel accommodation, catering, protection and security and other services.

Segment Sales Revenues

	External sales		Inter-segment		Total	
	2011	2010	2011	2010	2011	2010
Rubber products	38,255	35,969	301,192	430,611	339,447	464,580
Chemical products	103,848	183,856	30,269	(15,814)	134,117	168,042
Footwear	628	1,362	1,542,776	1,241,520	1,543,404	1,242,882
Trade	1,041,791	1,138,413	81,994	191,237	1,123,785	4,416,691
Services	881,326	707,932	118,712	173,727	1,000,038	881,659
Parent Company	<u>2,231,075</u>	<u>2,220,659</u>	<u>1,769,196</u>	<u>1,443,812</u>	<u>4,000,271</u>	<u>577,430</u>
Total	<u>4,296,923</u>	<u>4,288,181</u>	<u>3,844,139</u>	<u>3,465,093</u>	<u>8,141,062</u>	<u>7,753,284</u>
Eliminations					<u>(3,844,139)</u>	<u>(3,465,093)</u>
Consolidated sales revenues					<u><u>4,296,923</u></u>	<u><u>4,288,191</u></u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

6. OPERATING AND GEOGRAPHICAL SEGMENTS (Continued)

Segment Operating Result

	Year Ended December 31,	
	2011	2010
Rubber products	(137,070)	(30,951)
Chemical products	396	(58,036)
Footwear	173,898	6,891
Trade	22,287	24,792
Services	83,819	30,344
Parent Company	152,263	87,681
Total of all segments	295,593	60,721
Eliminations	(531,324)	(80,405)
Loss before taxation	(235,731)	(19,684)
Current income tax expense	(65,456)	(31,088)
Deferred income tax expense	(7,946)	(6,349)
Net (loss)	(309,133)	(57,121)

Segment Assets and Liabilities

	Assets		Liabilities	
	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010
Rubber products	1,307,922	1,120,619	937,260	820,247
Chemical products	273,816	271,303	142,415	140,271
Footwear	2,953,000	2,557,679	2,071,299	1,692,949
Trade	458,139	2,973,506	179,768	2,459,189
Services	870,524	887,855	341,011	378,858
Parent Company	7,421,327	4,278,197	4,531,862	1,448,936
Total of all segments	13,284,728	12,089,159	8,221,615	6,940,450
Eliminations	(4,381,085)	(3,868,607)	(2,557,060)	(2,248,259)
Consolidated	8,903,643	8,220,552	5,664,555	4,692,191

Other Segment Information

	Acquisition of fixed assets and intangible assets		Depreciation charges	
	2011	2010	2011	2010
Rubber products	92,235	130,230	25,575	20,492
Chemical products	20,592	16,948	1,950	4,416
Footwear	283,260	257,624	54,848	49,537
Trade	580	83,848	2,136	25,778
Services	22,120	49,526	27,488	27,506
Parent Company	176,766	93,213	49,977	25,309
	597,564	633,399	163,985	153,038

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***6. BUSINESS AND GEOGRAPHICAL SEGMENTS (Continued)*****Sale of Products, Goods and Services on Foreign Markets by Geographical Location***

	Year Ended December 31,	
	2011	2010
United Kingdom	852,850	899,727
Finland	373,368	321,982
Italy	259,372	336,889
Denmark	219,243	84,957
Sweden	145,076	71,174
Republic of Srpska	137,935	181,939
France	100,561	80,651
Macedonia	84,856	70,234
Montenegro	82,214	102,308
Russia	31,675	6,206
USA	21,829	33,682
Bulgaria	18,933	7,142
South Africa	15,173	35,414
Slovenia	14,346	17,563
Germany	13,666	6,769
China (Hong Kong)	10,720	0
Belgium	9,058	5,717
Poland	8,390	3,165
Other	47,430	91,511
	<u>2,446,695</u>	<u>2,357,030</u>

7. OWN WORK CAPITALIZED

Income from own work capitalized for the year ended December 31, 2011 aggregated to RSD 710,666 thousand (2010: RSD 743,239 thousand) mostly, in the amount of RSD 527,647 thousand (2010: RSD 526,258 thousand) refers to the costs of employee benefits directly attributed to property, plant and equipment and work in progress based on engagement in a number of projects with the view of improving business operations and developing new products, as well as adapting and reconstructing retail and servicing network. The Company's management believes that the aforementioned investments are necessary in order to improve business operation though increase in sales volume. Development of new products and reconstruction of retail stores and investments in developing servicing and distribution network for the purpose of direct sales to customers without intermediaries so as to achieve the highest margin percentage possible, whereof the management expects economic benefits in the ensuing years.

The remaining amount of RSD 183,019 thousand (2010: RSD 216,981 thousand) represents the effect of valuation of property the parent company transferred to its subsidiaries in order to increase capital contribution (Note 2.2.). The management construed the Opinion of Ministry of Finance dated January 22, 2009 on accounting for effects of the transfer of disposal rights over property from a parent company to its subsidiaries within capital increase procedure that is recorded as income as applicable to the consolidation level as well.

8. OTHER OPERATING INCOME

	Year Ended December 31,	
	2011	2010
Rentals	18,436	19,574
Other income	8,110	20,050
	<u>26,546</u>	<u>39,624</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***9. COST OF MATERIAL**

	Year Ended December 31,	
	2011	2010
Raw materials	1,607,889	1,299,477
Overheads	58,482	69,256
Electricity	54,014	53,447
Other fuel and energy costs	142,302	141,007
	<u>1,862,687</u>	<u>1,563,187</u>

10. STAFF COSTS

	Year Ended December 31,	
	2011	2010
Net salaries	1,020,304	925,030
Taxes and contributions on salaries paid by employees	380,378	342,712
Taxes and contributions on salaries paid by the employer	249,678	224,721
Considerations based on service contracts	11,600	10,658
Remunerations to the Management and Supervisory Boards	9,088	10,890
Retirement benefits and jubilee awards	1,255	1,778
Business travel costs and per diems	30,420	33,124
Employee transportation costs	57,236	54,469
Other staff costs	10,179	8,338
	<u>1,770,138</u>	<u>1,611,720</u>

11. DEPRECIATION, AMORTIZATION AND PROVISIONS

	Year Ended December 31,	
	2011	2010
Depreciation and amortization (Notes 19 and 20)	163,985	153,038
Long-term provisions (Note 30)	13,203	34,944
	<u>177,188</u>	<u>187,982</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***12. OTHER OPERATING EXPENSES**

	Year Ended December 31,	
	2011	2010
Other transportation services	224,482	166,383
Other non-production service costs	125,628	134,396
Rentals	73,769	79,009
Taxes and contributions	26,132	20,713
Telecommunications	22,297	18,933
Production costs	20,912	19,888
Other production services	19,963	17,101
Insurance premiums	19,568	20,647
Maintenance	19,209	24,666
Lawyer fees and other consultant services	18,399	18,670
Marketing and advertising	16,713	32,572
Bank charges	14,581	26,378
Entertainment	7,403	8,244
Fair exhibitions	5,427	4,920
Membership fees	2,110	2,583
Research	89	939
Other non-material expenses	21,940	28,473
	<u>638,622</u>	<u>624,515</u>

13. FINANCE INCOME

	Year Ended December 31,	
	2011	2010
Dividend income	-	72
Interest income from placements	3,451	3,000
Income from penalty interest	48	3,877
Foreign exchange gains	101,226	59,356
Other finance income	3,947	3,894
	<u>108,672</u>	<u>72,209</u>

14. FINANCE EXPENSES

	Year Ended December 31,	
	2011	2010
Interest expense	384,144	265,386
Foreign exchange losses	124,463	125,112
Other finance expenses	28,567	538
	<u>537,174</u>	<u>391,035</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***15. OTHER INCOME**

	Year Ended December 31,	
	2011	2010
Gains on the sales of property, plant and equipment	150,888	37,353
Effects of valuation of property held for sale	60,006	-
Reversal of long-term provisions (Note 30)	2,002	446
Reversal of allowance for impairment (Note 27)	1,110	5,701
Gains on the sale of materials	346	616
Surpluses	68	84
Write-off of liabilities	12	-
Collected receivable previously written off	-	8,101
Other income	23,228	22,204
	<u>237,660</u>	<u>74,505</u>

16. OTHER EXPENSES

	Year Ended December 31,	
	2011	2010
Losses on the sale of property, plant and equipment	1,671	30,931
Losses on sales of material	247	71
Shortages	290	66
Allowance for impairment of placements, receivables and inventories	12,496	3,934
Subsequently approved discounts and rebates to customers	24,959	4,106
Other expenses	18,159	11,646
	<u>57,822</u>	<u>46,648</u>

17. INCOME TAXES**a) Components of Income Taxes**

	2011	2010
Current income taxes	65,456	31,088
Deferred tax expense	7,946	6,349
	<u>73,402</u>	<u>37,437</u>

b) Numerical Reconciliation of the Tax Expense and the Product of Accounting Results as Multiplied by the Statutory Income Tax Rate

	2011	2010
Loss before taxation	(235,731)	(19,684)
Income taxes at the statutory tax rate of 10%	(23,573)	(1,968)
Tax effects of non-deductible expenses	88,377	38,724
Tax credits for capital expenditures	(24,787)	(3,828)
Tax loss carryforwards	15,668	-
Other	17,717	4,509
	<u>73,402</u>	<u>37,437</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

17. INCOME TAXES (Continued)

c) Components of Deferred Tax Assets and Liabilities

Deferred tax assets and liabilities relate to the following positions:

	<u>December 31, 2011</u>	<u>December 31, 2010</u>
Deferred tax assets		
Deferred tax assets arising from a difference between the value of assets recorded for book and tax purposes	22,160	21,305
Deferred tax liabilities		
Deferred tax liabilities arising on difference between the value of assets recorded for book and tax purposes	(142,966)	(134,696)
Deferred tax liabilities, net	<u>(120,806)</u>	<u>(113,391)</u>

d) Unrecognized Deferred Tax Assets

As of December 31, 2011, the Group did not recognize deferred tax assets arising from the earned tax credits that are available for carryforward, as the management was uncertain that these credits could be utilized in the future reporting periods.

<u>Inception Year</u>	<u>Expiration Year</u>	<u>December 31, 2011</u>	<u>December 31, 2010</u>
- 2003	2013	1,253	1,253
- 2004	2014	10,519	10,519
- 2005	2015	2,271	2,271
- 2006	2016	2,558	2,558
- 2007	2017	8,627	8,627
- 2008	2018	82,364	82,364
- 2009	2019	62,888	62,888
- 2010	2015	33,534	37,632
- 2011	2021	181,424	-
	Used in the current year:	<u>(24,787)</u>	<u>(3,828)</u>
		<u>356,823</u>	<u>204,014</u>

18. EARNINGS PER SHARE

	<u>2011</u>	<u>2010</u>
Net loss	(309,133)	(57,121)
Weighted average number of shares in the year	<u>1,718,460</u>	<u>1,718,460</u>
Earnings per share (in RSD)	<u>(179.89)</u>	<u>(33.24)</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

19. INTANGIBLE ASSETS

	Licenses	Other Intangible Assets	Intangible Assets in Progress	Total Intangible Assets
Cost				
Balance, January 1, 2010	19,503	1,273	106,080	126,856
Additions	5,381	-	403,635	409,016
Transfers	7,003	(152)	(6,851)	-
Other	-	-	(120,380)	(120,380)
Balance, December 31, 2010	<u>31,887</u>	<u>1,121</u>	<u>382,484</u>	<u>415,492</u>
Balance, January 1, 2011	31,887	1,121	382,484	415,492
Additions	-	563	414,436	414,999
Transfers	(361)	197,731	(199,141)	(1,771)
Transfer to property and equipment	-	-	(260,520)	(260,520)
Balance, December 31, 2011	<u>31,526</u>	<u>199,415</u>	<u>337,259</u>	<u>568,200</u>
Accumulated Amortization				
Balance, January 1, 2010	14,255	1,160	-	15,415
Charge for the year	2,002	(50)	-	1,952
Balance, December 31, 2010	<u>16,257</u>	<u>1,110</u>	<u>-</u>	<u>17,367</u>
Balance, January 1, 2011	16,257	1,110	-	17,367
Charge for the year	3,245	437	-	3,682
Balance, December 31, 2011	<u>19,502</u>	<u>1,547</u>	<u>-</u>	<u>21,049</u>
Net Book Value				
- December 31, 2011	<u>12,024</u>	<u>197,868</u>	<u>337,259</u>	<u>547,151</u>
- December 31, 2010	<u>15,630</u>	<u>11</u>	<u>382,484</u>	<u>398,125</u>

Intangible assets in progress stated in the amount of RSD 337,259 thousand mostly refer to the following:

	<u>2011</u>	<u>2010</u>
Development of new footwear products	313,353	229,936
Information technologies	-	9,242
Other	<u>23,906</u>	<u>121,969</u>
	<u>337,259</u>	<u>382,484</u>

The Group's management expects future economic benefits resulting from the projects presented through extended range of sales products and penetration into new markets.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

20. PROPERTY, PLANT AND EQUIPMENT

	Land	Buildings	Plant and Equipment	Other Assets	Advances and Construction in Progress	Total	Investment Property
Cost							
Balance, January 1, 2010	122,411	2,711,736	1,398,120	24,318	208,020	4,464,605	-
Additions	-	-	-	-	108,039	108,039	-
Transfer from intangible assets	-	44,729	63,001	-	120,380	228,110	-
Valuation effect	586	110,599	-	-	106,392	217,577	-
Other	-	(6,962)	(1,805)	-	-	(8,767)	-
Sale and disposal	(171)	(130)	(39,120)	-	(28,601)	(68,022)	-
Balance, December 31, 2010	<u>123,937</u>	<u>2,950,131</u>	<u>1,597,092</u>	<u>28,395</u>	<u>241,987</u>	<u>4,941,542</u>	<u>-</u>
Balance, January 1, 2011	123,937	2,950,131	1,597,092	28,395	241,987	4,941,542	-
Additions	-	187,099	-	1,618	402,537	591,254	-
Activation	-	65,477	51,577	2,148	(119,202)	-	-
Transfer from intangible assets	-	-	45,089	-	215,431	260,520	-
Valuation effect	13,244	55,969	-	-	-	69,211	-
Transfer to assets held for sale and intangible assets	-	(233,585)	(272)	-	-	(233,857)	227,011
Sale and disposal	(48,164)	(244,582)	(30,234)	(3,919)	-	(326,899)	-
Balance, December 31, 2011	<u>89,017</u>	<u>2,780,509</u>	<u>1,663,252</u>	<u>28,242</u>	<u>740,753</u>	<u>5,301,773</u>	<u>227,011</u>
Accumulated Depreciation							
Balance, January 1, 2010	-	85,813	435,048	3,806	-	524,667	-
Charge for the year	-	30,838	116,999	3,249	-	151,086	-
Other	-	4,647	-	-	-	4,647	-
Sale and disposal	-	-	(26,972)	-	-	(25,586)	-
Balance, December 31, 2010	<u>-</u>	<u>121,298</u>	<u>525,075</u>	<u>7,055</u>	<u>-</u>	<u>653,428</u>	<u>-</u>
Balance, January 1, 2011	-	121,298	525,075	7,055	-	653,428	-
Charge for the year	-	52,115	103,021	5,167	-	160,303	-
Sale and disposal	-	(25,186)	(7,531)	(725)	-	(33,442)	-
Balance, December 31, 2011	<u>-</u>	<u>148,227</u>	<u>620,565</u>	<u>11,497</u>	<u>-</u>	<u>780,289</u>	<u>-</u>
Net Book Value							
- December 31, 2011	<u>89,017</u>	<u>2,632,282</u>	<u>1,042,687</u>	<u>16,745</u>	<u>740,753</u>	<u>4,521,484</u>	<u>227,011</u>
- December 31, 2010	<u>123,937</u>	<u>2,828,833</u>	<u>1,072,017</u>	<u>21,340</u>	<u>241,987</u>	<u>4,288,114</u>	<u>-</u>

A first ranking mortgage lien has been placed in favor of Alpha Bank A.D., Beograd against the Company's buildings and factory courtyard, and serves to securitize the regular repayment of refinanced foreign currency loans. In accordance with the terms of the Agreement on Rescheduling and Write-off of Principal and Interest, executed on October 6, 2004 with Alpha Bank A.D., Beograd, the outstanding portion of such loans at December 31, 2010 amounted to EUR 793,540 and USD 599,114 or RSD 131,485 thousand as translated to dinars (Note 31).

Over buildings used to perform other industries located on the cadaster lot number 3620/1 inscribed in the title deed number 8370 of the Cadastral Municipality of Pirot (of the aggregate net book value as of December 31, 2011 of RSD 434,067 thousand) a pledge lien has been instituted in favor of Banca Intesa a.d., Beograd based on a long-term loan approved on March 5, 2010 in the amount of RSD 150,000 thousand, whereof the amount outstanding as of December 31, 2011 totaled RSD 93,750 thousand (Note 31). In addition, The June 21, 2010 Pledge Lien Agreement instituted a pledge lien over certain Company's equipment in favor of Banca Intesa a.d., Beograd to securitize the aforementioned loan.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***20. PROPERTY, PLANT, EQUIPMENT AND INVESTMENT PROPERTY (Continued)**

Over properties of the new footwear production plant (of the net book value as of December 31, 2011 of RSD 774,436 thousand) first ranking mortgage lien was instituted in favor of DEG (Deutsche Investitions und Entwicklungsgesellschaft mbh), Frankfurt, Germany, as well as first ranking pledge over all present and future equipment and movables of the subsidiary Tigar Obuca d.o.o., Pirot, whose portion as of December 31, 2011 amounted to RSD 732,486 thousand (Note 31).

In addition, pledge lien was instituted over a number of the Company's buildings located across the Republic in favor of commercial banks to securitize repayment of long-term and short-term loans.

Construction in progress in the amount of RSD 740,753 thousand mostly relate to the following:

	<u>2011</u>	<u>2010</u>
Facilities and properties at the Kartonaza location	141,857	-
Investments in fixed assets for production of technical rubber products	217,532	49,883
Investments in fixed assets for production of chemical products	108,255	119,571
New chemical products production plant	32,538	21,337
Development of new chemical products	31,909	-
Development of new technical rubber products	61,111	-
Information technologies	19,889	-
Development of retail and servicing network	74,019	51,196
Other	53,643	-
	<u>740,753</u>	<u>241,987</u>

Facilities and properties at the Kartonaza location are intended for storage, whereas, due to their excellent location and connections to main roads, the facilities will be used for construction of modern multi-purpose logistics center, by the highest standards, for all production programs, as well as the goods of other manufacturers traded in both domestic and foreign markets.

Investments in property, plant and equipment for production of chemicals and technical rubber products relate to the location Tigar 3 and footwear, technical rubber and recycled products production plants that are, in the management's opinion, necessary for further development and improvement of production process.

21. EQUITY INVESTMENTS

	<u>December 31, 2011</u>	<u>December 31, 2010</u>
Equity investments in other legal entities	13,300	13,300
Less: Allowance for impairment (Note 27)	(1,481)	(1,481)
	<u>11,819</u>	<u>11,819</u>

22. OTHER LONG-TERM FINANCIAL PLACEMENTS

Other long-term financial placements stated in the consolidated balance sheet as of December 31, 2011, in the amount of RSD 41,720 thousand (December 31, 2010: RSD 45,468 thousand) relate to the receivables from employees based on the approved long-term housing loans, with up to 20-year maturities effective from the execution date of the loan agreement, and issued at annual interest rates ranging from 1.5% to 2%.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***23. INVENTORIES**

	December 31, 2011	December 31, 2010
Raw materials and other materials	209,162	229,565
Spare parts	33,979	30,203
Work in progress	479,231	310,740
Finished products	1,086,620	990,761
Goods	214,864	208,309
Advances to suppliers	51,229	64,564
	<u>2,075,085</u>	<u>1,834,142</u>
Less: Allowance for impairment of inventories (Note 27)	<u>(1,798)</u>	<u>(10,496)</u>
	<u><u>2,073,287</u></u>	<u><u>1,823,646</u></u>

Finished products and goods stated in the amount of RSD 1,301,484 thousand relate to the following:

	December 31, 2011	December 31, 2010
Technical rubber products	307,797	321,396
Chemical products	49,940	39,520
Footwear	728,883	629,845
Total finished goods	<u>1,086,620</u>	<u>990,761</u>
Goods		
- Automobile tyres	105,299	101,075
- other goods	109,565	107,234
Total goods	<u>214,864</u>	<u>208,309</u>
	<u><u>1,301,484</u></u>	<u><u>1,199,070</u></u>

The rise in prices of natural rubber and textile in the global market starting from 2011 resulted in a two-digit and, in some instances, a three-digit increase in all sorts of goods from the Group's product range in the global market. In addition, modern technologies and materials applied in the production process prevent any damages or deformation of the products due to retention, as well as any adverse effect on their functionality. The inventory turnover does not depart from the standards and practices of distributors worldwide; therefore the Group's management deems that the inventories of goods will be realized in the ensuing periods, as well as that the recoverable value of inventories will not be below the stated present value of inventories, i.e. that the stated allowance for impairment in the amount of RSD 1,798 thousand is sufficient.

Inventories comprise inventories of footwear (low-cut footwear, work footwear, hunting and fishing rubber boots, protective and special-purpose footwear, as well as fashion footwear), technical rubber (pressed rubber products, profiles and pipes, sports program, industrial rubber and recycled rubber products), chemical products (consumer glues, industrial glues and adhesives, consumer and industrial colors and lacquers, polyurethane floors, solvents and auxiliary chemicals) and other products.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.*

24. NON-CURRENT ASSETS HELD FOR SALE	December 31, 2011	December 31, 2010
Property held for sale	6,574	19,321
Equipment held for sale	272	718
	<u>6,846</u>	<u>20,039</u>
25. ACCOUNTS RECEIVABLE	December 31, 2011	December 31, 2010
Receivables from related parties	60,203	42,743
Domestic accounts receivable	474,574	519,863
Foreign accounts receivable	351,096	327,680
Prepaid other taxes and contributions	71	216
Receivables from employees	29,359	29,548
Other receivables	16,390	11,997
	<u>931,693</u>	<u>932,047</u>
Less: Allowance for impairment of receivables (Note 27)	<u>(38,735)</u>	<u>(28,885)</u>
	<u>892,958</u>	<u>903,162</u>
26. CASH AND CASH EQUIVALENTS	December 31, 2011	December 31, 2010
Cash on hand in RSD	5,170	3,210
Cash on hand in foreign currency	44	18,718
Business account in RSD	3,588	7,430
Business account in foreign currency	49,733	115,099
Other cash	187,095	219,399
Securities and cash equivalents	5,463	5,668
	<u>251,093</u>	<u>369,524</u>

Other cash includes short-term guarantee deposits stated at December 31, 2011 in the total amount of RSD 145,465 thousand (EUR 1,300,000 and RSD 25,000 thousand) that have been placed with commercial banks for the purpose of securing short-term loans approved and banking guarantees issued – AIK Banka a.d., Beograd (RSD 25,000 thousand), EFG a.d., Beograd (RSD 50,758 thousand), Hypo Alpe Adria Bank a.d., Beograd (RSD 17,387 thousand), Societe Generale Banka Srbija a.d., Beograd (RSD 20,928 thousand) and Srpska banka a.d., Beograd (RSD 31,392 thousand).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

27. MOVEMENTS IN PROVISIONS

	Equity Investments (Note 21)	Inventories (Note 23)	Accounts Receivable (Note 25)	Total
Balance, January 1, 2010	1,481	3,286	35,359	40,126
Gains on the valuation adjustments (Note 15)	-	-	(5,701)	(5,701)
Charge for the year (Note 16)	-	3,934	-	3,934
Other	-	3,276	(773)	2,503
Balance, December 31, 2010	1,481	10,496	28,885	40,862
Gains on the valuation adjustments (Note 15)	-	-	(1,110)	(1,110)
Charge for the year (Note 16)	-	1,536	10,960	12,496
Derecognition	-	(10,234)	-	(10,234)
Balance, December 31, 2011	1,481	1,798	38,735	42,014

28. VALUE ADDED TAXES AND PREPAYMENTS

	December 31, 2011	December 31, 2010
Receivables for prepaid VAT	40,793	49,432
Prepaid expenses	1,640	941
Other prepayments	81,039	96,736
Deferred unrealized foreign exchange losses, net	177,706	180,158
	301,178	327,267

29. SHARE CAPITAL

According to the excerpt from the Central Securities Depository and Clearing House, the ownership structure of the Company's share capital as of December 31, 2011 was as follows:

	Number of Shares	%	Thousands of RSD
Share Fund of the Republic of Serbia	429,429	25.0	515,315
Pension and Disability Fund of the Republic of Serbia	168,462	9.0	179,977
Erste Bank a.d., Novi Sad – Custody	127,999	7.0	153,599
Société Générale Bank Srbija a.d., Beograd – Custody	104,947	6.0	125,936
Unicredit bank Srbija a.d – Custody	75,503	4.0	90,604
Raiffeisenbank a.d., Beograd – Custody	52,505	3.0	63,006
Raiffeisenbank a.d., Beograd – Custody	49,851	3.0	59,821
Komercijalna Banka a.d., Beograd – Custody	26,062	2.0	31,274
Herma Investments Co. Ltd.	20,000	1.0	24,000
Unicredit bank Srbija a.d – Custody	19	1.0	22,200
Other	663,683	39.0	796,420
	1,718,460	100.0	2,062,152

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***29. SHARE CAPITAL (Continued)**

According to the excerpt from the Central Securities Depository and Clearing House, the ownership structure of the Company's share capital as of December 31, 2010 was as follows:

	<u>Number of Shares</u>	<u>%</u>	<u>Thousands of RSD</u>
Share Fund of the Republic of Serbia	429,429	25.0	515,315
Pension and Disability Fund of the Republic of Serbia	149,981	9.0	179,977
Artio International Equity Fund	123,132	7.0	147,758
Erste Bank a.d., Novi Sad – Custody	87,728	5.0	105,274
Société Générale Bank Srbija a.d., Beograd – Custody	55,654	3.0	66,785
Raiffeisenbank a.d., Beograd – Custody	42,164	2.0	50,597
Erste & Streiermarkische Bank d.d.	37,637	2.0	45,164
Komercijalna Banka a.d., Beograd – Custody	26,062	2.0	31,274
Sweden Bank a.s.	24,851	1.0	29,821
UniCredit Bank a.d., Beograd	18,500	1.0	22,200
Other	723,322	43.0	867,986
	<u>1,718,460</u>	<u>100.0</u>	<u>2,062,152</u>

As of December 31, 2011 and 2010, the Company's share capital comprised of 1,718,460 ordinary shares with the individual par value of RSD 1,200.

Based on the Decision of the Company's Assembly dated June 24, 2011, the Company distributed prior years' profit in the form of dividend paid to shareholders in the total of RSD 37,895 thousand.

30. LONG-TERM PROVISIONS

Long-term provisions which amounted to RSD 84,127 thousand as of December 31, 2011 (December 31, 2010: RSD 83,087 thousand) entirely relate to long-term provisions for employee retirement benefits and jubilee awards.

The assumptions used in the actuarial assessment were as follows:

	<u>2011</u>	<u>2010</u>
Nominal discount rate	9.75%	11.5%
Expected rate of nominal salary growth	7%	8%

The amounts included in the consolidated balance sheet with respect to a defined benefit plan are as follows:

	<u>December 31, 2011</u>	<u>December 31, 2010</u>
Balance, January 1	81,376	78,631
Additional provisions (Note 11)	13,203	34,944
Reversal of long-term provisions (Note 15)	(2,002)	(446)
Employee retirement benefits	(8,450)	(29,357)
Other changes	-	(685)
Balance, December 31	<u>84,127</u>	<u>83,087</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

31. LONG-TERM LIABILITIES

	December 31, 2011	December 31, 2010
Long-term bonds	290,292	243,763
Long-term borrowings		
- foreign	863,971	931,811
- domestic	855,820	1,039,796
Finance lease liabilities	21,412	34,268
	2,031,495	2,249,638
Less: Current portions (Note 32)	(761,386)	(520,357)
	<u>1,270,109</u>	<u>1,729,282</u>

a) Long-Term Bonds

<u>Investor</u>	Annual Interest Rate	Currency		December 31, 2011	December 31, 2010
		Code	Amount		
Komercijalna banka a.d., Beograd	7.5 %	EUR	958,703	82,127	101,142
Wiener Stadtische osiguranje a.d., Beograd	7.5 %	EUR	678,895	58,383	71,622
KBC Banka a.d., Beograd	7.5 %	EUR	199,543	47,810	21,051
DDOR Novi Sad a.d., Novi Sad	7.5 %	EUR	188,248	36,666	19,860
Takovo a.d., Kragujevac	7.5 %	EUR	185,429	26,155	19,562
Wiener reosiguranje a.d., Beograd	7.5 %	EUR	99,772	18,823	10,526
Jubmes Banka a.d. Beograd	9.0%	EUR	194,256	20,327	-
				<u>290,292</u>	<u>243,763</u>
Less: Current portion of long-term bonds				(59,991)	(43,314)
				<u>230,301</u>	<u>200,449</u>

The maturities of long-term bonds are as follows:

	December 31, 2011	December 31, 2010
Within a year	59,991	43,314
From 1 to 5 years	<u>230,301</u>	<u>200,449</u>
	<u>290,292</u>	<u>243,763</u>

In 2011, the Company executed the third private bond issue to known buyers, without public offering. The total number of bonds issued was 34,500, worth RSD 340,395 thousand; bonds accrue interest at the 7.5% rate annually, are indexed to a currency clause and mature over a period of five years.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

31. LONG-TERM LIABILITIES (Continued)

b) Long-Term Borrowings, Domestic

<u>Creditor</u>	<u>Annual Interest Rate</u>	<u>Currency Code</u>	<u>Currency Amount</u>	<u>December 31, 2011</u>	<u>December 31, 2010</u>
Banca Intesa ad ,Beograd	1.2% p.m.	RSD		93,750	150,000
Hypo Aple Adria ad, Beograd	3M EURIBOR + 8.5% p.a.	EUR	2,000,000	188,919	211,629
Hypo Aple Adria ad, Beograd	3M EURIBOR + 8.5% p.a.	EUR	500,000	28,624	52,907
Hypo Aple Adria ad, Beograd	3M EURIBOR + 8.5% p.a.	EUR	500,000	28,624	52,907
Hypo Aple Adria ad, Beograd	3M EURIBOR + 7% p.a.	EUR	2,500,000	244,894	264,537
Hypo Aple Adria ad, Beograd	3M EURIBOR + 8% p.a.	EUR	915,000	89,632	96,820
Erste Bank, ad Beograd	3.1% p.a.	EUR	2,000,000	181,377	210,996
				<u>855,820</u>	<u>1,039,796</u>
Less: Current portion of long-term borrowings				<u>(514,160)</u>	<u>(242,132)</u>
				<u>341,660</u>	<u>436,668</u>

c) Long-Term Borrowings, Foreign

<u>Creditor</u>	<u>Annual Interest Rate</u>	<u>Currency Code</u>	<u>Currency Amount</u>	<u>December 31, 2011</u>	<u>December 31, 2010</u>
Refinanced loans through Alpha bank A.D., Beograd:					
Berliner Bank A.G., Berlin	5.5 % p.a.	EUR	178,644	18,694	27,768
Algemeine bank Netherlands, Amsterdam,	5.6 % p.a.	EUR	614,895	64,343	95,576
The First National Bank, Chicago, USA	5.5 % p.a.	USD	599,114	48,448	69,980
				<u>131,485</u>	<u>193,324</u>
DEG (Deutsche Investitions und Entwicklungsgesellschaft mbh), Frankfurt, Germany	6 M EURIBOR + 2.875% p.a.	EUR	7,000,000	732,486	738,487
				<u>863,971</u>	<u>931,811</u>
Less: Current portion of long-term borrowings				<u>(173,159)</u>	<u>(62,109)</u>
				<u>690,812</u>	<u>869,702</u>

Long-term financial liabilities as of December 31, 2011 of RSD 732,486 thousand (December 31, 2010: RSD 738,487 thousand), entirely refer to the liabilities to DEG (Deutsche Investitions und Entwicklungsgesellschaft mbh), Frankfurt, Germany, based on a long-term loan. In 2008, the company entered into the Agreement on Long-Term Financing (the "Agreement") with DEG (Deutsche Investitions und Entwicklungsgesellschaft mbh), Frankfurt, Germany, for the purpose of reallocation of production into the new production plant, purchase of machinery and acquisition of rights to brands belonging to Hunter Boot Ltd., UK. The maximum financing amount pursuant to the Agreement as of October 14, 2008 totals EUR 7 million, with principal repayment in equal semi-annual installments, the first of which is due at September 15, 2012 and the last one at March 15, 2016. The interest rate equals 6-month EURIBOR + 2.875% annually, and the interest accrued is calculated to the outstanding loan amount and paid in semi-annual payments.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

31. LONG-TERM LIABILITIES (Continued)

c) Long-Term Borrowings, Foreign (Continued)

As collateral, ten blank bills of exchange were deposited covering the loan amount and financing costs. In addition, first ranking mortgage lien was instituted in favor of the creditor over a new production plant, first ranking pledge over all present and future equipment and movables as well as over all accounts receivable within the records of the subsidiary Tigar Obuca d.o.o., Pirot. The value of aggregate pledge must at all times equal 150% of the amount of the liability to the creditor.

Pursuant to the Agreement, the Company is obligated to adhere to the maximum and minimum adequacy ratios during loan repayment, as follows:

- equity ratio – minimum 30%;
- current ratio – minimum 1.2;
- debt service coverage ratio – minimum 1.3.

As of December 31, 2011, two of the three financial indicators (equity ratio – 29.5% and current ratio – 0.6%) were not in compliance with the conditions defined in the Agreement with DEG (Deutsche Investitions und Entwicklungsgesellschaft mbh), Frankfurt, Germany, which, among other issues, allows the creditor to request early loan repayment. Given that, up to the date of approval of this report, the creditor had not delivered repayment reminders or requested early repayment loan, the Group's management holds that as of December 31, 2011 there are no grounds for any reclassification of the recorded long-term liabilities into short-term liabilities.

In accordance with interpretations of the Agreement provisions, the subsidiary compiled a methodology for calculation of the abovementioned ratios, whereto the creditor consented and whereby the Company fulfills the debt service coverage ratio requirement as of December 31, 2011.

d) Finance Lease Liabilities

	Sum of		Present Value of	
	Minimum Lease Payments December 31, 2011	December 31, 2010	Minimum Lease Payments December 31, 2011	December 31, 2010
<i>Maturity:</i>				
Up to one year	15,350	20,651	14,076	18,104
From 1 to 5 years	7,614	16,925	7,336	16,154
	22,964	37,576	21,412	34,268
Less: future cost of financing	(1,552)	(3,308)	-	-
Present value of minimum lease payments	21,412	34,268	21,412	34,268
Included in the financial statements as:				
Current portion of long-term liabilities			14,076	18,104
Other long-term liabilities			7,336	16,154
			21,412	34,268

Maturities of long-term liabilities are presented in the following table:

	December 31, 2011	December 31, 2010
- within a year (Note 32)	761,386	520,357
- from 1 to 5 years	1,270,109	1,729,282
	2,031,495	2,249,639

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

32. SHORT-TERM FINANCIAL LIABILITIES

	December 31, 2011	December 31, 2010
Short-term loans, domestic	1,866,210	1,165,758
Current account overdrafts	26,606	30,095
Short-term bonds issued	30,000	-
Current portions of long-term financial liabilities (Note 31)	761,386	520,357
	<u>2,684,202</u>	<u>1,716,210</u>

a) Short-Term Loans, Domestic

Creditor	Interest Rate	Code	Currency		
			Amount	December 31, 2011	December 31, 2010
<u>Loans in foreign currency:</u>					
AOFI Beograd	5% p.a.	EUR	500,000	52,320	52,749
Banca Intesa a.d. Beograd	9% p.a.	EUR	2,000,000	209,282	-
Banca Intesa a.d. Beograd	9% p.a.	EUR	137,368	14,404	-
Banca Intesa a.d. Beograd	10% p.a.	EUR	592,000	61,948	-
Univerzal banka a.d., Beograd	1% p.m.	EUR	500,000	52,320	-
	3-m EURIBOR +				-
Societe General bank a.d.	5.3% p.a.	EUR	2,800,000	292,995	-
	3-m EURIBOR +				-
Societe General bank a.d.	5% p.a.	EUR	500,000	52,320	-
	3-m EURIBOR +				-
„Eurobank EFG a.d., Beograd	6.5% p.a.	EUR	1,000,000	104,641	-
AIK banka a.d. Niš		EUR	2,000,000	-	210,996
AIK banka a.d. Niš		EUR	300,000	-	29,382
Societe General bank a.d.		EUR	2,000,000	-	211,630
Banca Intesa a.d. Beograd		EUR	875,000	-	92,312
Societe General bank a.d.		EUR	480,000	-	50,639
Societe General bank a.d.		EUR	800,000	-	84,399
Hypo Alpe Adria Banka a.d.		EUR	286,000	-	30,264
				<u>840,230</u>	<u>762,371</u>
<u>Loans in RSD:</u>					
	from 1.7% p.m. to 3.5% + RKS NBS p.a.			255,637	-
AIK banka ad Niš				510,000	-
Srpska banka ad Beograd	from 1.6% p.m.			65,000	-
Univerzal banka a.d., Beograd	7% p.a.			30,000	-
Privredna banka a.d., Beograd	12.25% p.a.			51,500	-
Dunav banka a.d., Zvečan	20.25% p.a.			99,379	-
Societe Generale a.d.	1m BELIBOR + 1.9%			-	180,000
Srpska banka a.d.				-	70,428
Unicredit banka a.d., Beograd				-	85,014
Privredna banka a.d., Beograd				-	45,000
Societe Generale a.d.				-	4,500
Unicredit banka a.d., Beograd				-	2,694
AIK Banka				-	14,464
Other				1,025,980	403,387
				<u>1,866,210</u>	<u>1,165,758</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

32. SHORT-TERM FINANCIAL LIABILITIES (Continued)

b) Current Account Overdrafts

<u>Creditor</u>	<u>Interest Rate</u>	<u>December 31, 2011</u>	<u>December 31, 2010</u>
Privredna banka a.d., Beograd	19% p.a.	19,999	19,983
Unicredit banka a.d., Beograd	1m BELIBOR+2.15% p.a.	6,607	10,112
		<u>26,606</u>	<u>30,095</u>

c) Short-Term Bonds Issued

Short-term bonds issued in the amount of RSD 30,000 thousand mature as of March 27, 2012 (Investor Wiener Stadtische osiguranje a.d., Beograd). The bonds were issued in several issues at the interest rate ranging from 2% to 9% annually.

33. ACCOUNTS PAYABLE

	<u>December 31, 2011</u>	<u>December 31, 2010</u>
Accounts payable – related parties	37,636	19,236
Advances, deposits and retainers	59,680	89,556
Accounts payable – domestic	664,856	547,353
Accounts payable – foreign	386,127	181,306
Other accounts payable	16,208	13,694
	<u>1,164,507</u>	<u>851,145</u>

34. OTHER CURRENT LIABILITIES

	<u>December 31, 2011</u>	<u>December 31, 2010</u>
Gross salaries	201,866	139,434
Interest accrued	34,526	20,984
Liabilities for dividends and share in profit	53,343	16,696
Other current liabilities	6,697	6,812
	<u>296,432</u>	<u>183,926</u>

35. VAT AND OTHER PUBLIC DUTIES PAYABLE AND ACCRUALS

	<u>December 31, 2011</u>	<u>December 31, 2010</u>
VAT payables	8,132	38,523
Other taxes and contributions payable	10,939	5,639
Accrued expenses	84,550	63,283
Deferred income	-	667
Other accruals	11,231	2,343
	<u>114,852</u>	<u>110,455</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***36. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT****Capital Risk Management**

There is no legal framework for managing capital risk in the Company i.e. the Group. The Group's management considers capital risk in order to diminish it and under the assumption that the Company will be able to continue its business operations in the foreseeable future, maximizing profits to the owners by optimizing the debt to equity ratio. The structure of the Company's and the Group's capital includes debts, including long-term borrowings explained in Notes 31 and 32, other long-term liabilities, cash and cash equivalents and equity attributed to owners which entails share capital, other capital, reserves, as well as retained earnings. Based on such review, the Group balances the equity structure through the payment of dividends, new long-term investments, as well as by obtaining new borrowings and repurchase of the existing ones.

The persons controlling finances on the Group level review the equity structure on annual basis. As a part of the review, the Group's management considers equity price and risk relating to the type of capital.

The gearing ratios of the Group as of the year-end were as follows:

	December 31, 2011	December 31, 2010
Debt a)	3,954,311	3,445,492
Cash and cash equivalents	<u>(251,093)</u>	<u>(369,524)</u>
Net debt	<u>3,703,218</u>	<u>3,075,968</u>
Equity b)	<u>3,096,122</u>	<u>3,393,665</u>
Debt-to-equity ratio	<u>1.20</u>	<u>0.91</u>

a) Debt is related to long-term and short-term borrowings and other financial liabilities.

b) Equity includes share capital, share premium, reserves, as well as loss and retained earnings.

Significant Accounting Policies Regarding Financial Instruments

The review of significant accounting policies, including the basis for measurement and recognition of income and expenses for each category of financial assets and financial liabilities, are set out in Note 3 to the financial statements.

Categories of Financial Instruments

	December 31, 2011	December 31, 2010
Financial assets		
Long-term financial placements	41,720	45,468
Accounts receivable	847,138	861,401
Other receivables	45,820	41,761
Cash and cash equivalents	251,093	369,524
Short-term financial placements	<u>4,765</u>	<u>4,986</u>
	<u>1,190,536</u>	<u>1,323,140</u>
Financial liabilities		
Long-term borrowings	1,270,109	1,729,282
Accounts payable and other payables	1,104,827	851,145
Current portion of long-term liabilities	761,386	520,358
Short-term financial liabilities	<u>1,922,816</u>	<u>1,195,851</u>
	<u>5,059,138</u>	<u>4,296,636</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***35. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)****Categories of Financial Instruments (Continued)**

The Group's basic financial instruments comprise cash and cash equivalents, receivables, long-term and short-term financial placements related to the Company's business operations, as well as long-term borrowings, accounts payable and other liabilities mainly intended to finance the Group's current operations. In the regular course of business, the Group is exposed to the risk enumerated in the following passages.

Objectives of Financial Risk Management

Financial risks include market risk (foreign currency and interest rate risk), credit risk and liquidity risk. Financial risks are considered on time basis and are primarily mitigated by reducing the Group's exposure to these risks. The Group does not make use of any financial instruments as a hedge against the effects of financial risks on business operations because such instruments are neither widely used, nor is there an organized market for such instruments in the Republic of Serbia.

Market Risk

In its business operations, the Group is exposed to financial risks inherent in foreign currency and interest rate changes.

There were significant changes neither in the exposure of the Group to market risk, nor in the manner in which the Group manages or measures that risk.

Foreign Currency Risk

The Group is mainly exposed to the foreign currency risk through the items of cash and cash equivalents, accounts receivable, long-term borrowings and accounts payable denominated in foreign currency. The Group does not use special hedge instruments, since such instruments are uncommon in the Republic of Serbia. The stability of the economic environment in which the Group operates largely depends upon the economic measures introduced by the Government and the establishment of an adequate legal and regulatory framework.

The carrying value of the Group's monetary assets and liabilities expressed in foreign currency as of the reporting date were as follows:

	Assets		Liabilities	
	December 31, 2011	December 31, 2010	December 31, 2011	December 31, 2010
EUR	206,692	413,168	2,819,027	2,884,546
USD	2,100	2,550	229,015	93,627
GBP	11,666	14,890	2,484	645
CHF	-	-	-	324
	<u>220,458</u>	<u>430,608</u>	<u>3,050,526</u>	<u>2,979,142</u>

The Group is sensitive to the movements in the Euro (EUR) and American Dollar (USD) exchange rates. The following table gives details on the Company's sensitivity to the increase and decrease of 10% in the dinar against foreign currency exchange rate. The sensitivity rate of 10% was used in internal reporting on the foreign currency risk and it represents the management's best estimate of reasonably expected fluctuations in exchange rates. The sensitivity analysis includes only the outstanding foreign currency assets and liabilities and it adjusts their translation at the period end for the fluctuation of 10% in foreign exchange rates. The positive number from the table indicates the increase in the results of the current period, being the case when RSD value rises against the currency at issue. In case of RSD decline by 10% as compared to the relevant foreign currency, the impact on the profit for the current period would be the exact opposite of the one calculated in the previous case.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

35. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)

Market risk (Continued)

Foreign Currency Risk (Continued)

	31.decembar 2011	December 31, 2010
EUR	261,233	247,138
USD	22,691	9,107
GBP	(918)	(1,425)
CHF	-	32
	<u>283,006</u>	<u>254,852</u>
Impact on net profit for the year	<u>283,006</u>	<u>254,852</u>

The Group's sensitivity to the movements in foreign currency increased in the current period, primarily as a consequence of nominal increase of liabilities stated in EUR, mostly long-term loans.

Interest Rate Risk

The Company is exposed to interest rate risk inherent in assets and liabilities with floating interest rate. This risk depends upon the financial market and the Company does not have any instruments that could alleviate its influence.

The carrying values of financial assets and liabilities at the end of the period under review are presented in the following table:

	December 31, 2011	December 31, 2010
Financial Assets		
<i>Non-interest bearing</i>		
Accounts receivable	847,138	861,401
Other receivables	45,820	41,761
Cash and cash equivalents	63,998	150,125
Short-term financial placements	4,765	4,986
	<u>961,721</u>	<u>1,058,273</u>
<i>Fixed interest rates</i>		
Long-term financial placements	41,720	45,468
Cash and cash equivalents	187,095	219,399
	<u>228,815</u>	<u>264,867</u>
	<u>1,190,536</u>	<u>1,323,140</u>
Financial liabilities		
<i>Non-interest bearing</i>		
Accounts payable and other payables	1,104,827	851,145
<i>Fixed interest rates</i>		
Long-term borrowings	297,474	454,579
Short-term borrowings	1,232,813	763,808
Current portion of long-term liabilities	412,043	374,914
	<u>1,942,330</u>	<u>1,593,301</u>
<i>Variable interest rates</i>		
Long-term borrowings	972,635	1,274,702
Short-term borrowings	690,003	432,043
Current portion of long-term liabilities	349,343	145,445
	<u>2,011,981</u>	<u>1,852,190</u>
	<u>5,059,138</u>	<u>4,296,636</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

35. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)

Market risk (Continued)

Interest Rate Risk (Continued)

The sensitivity analyses presented in the following text have been established based on the Company's exposure to interest rate risk inherent in non-derivative instruments as of the balance sheet date. For the liabilities with variable interest rate, the analysis has been prepared under the assumption that the outstanding balance of assets and liabilities as of the balance sheet date remained constant throughout the year. The 1% increase or decrease in interest rates represents the fluctuation reasonably anticipated by management. Had the interest rates been 1% higher and other variables remained unchanged, the Group would have incurred an operating loss in the year ended December 31, 2011 in the amount of RSD 20,120 thousand (December 31, 2010: RSD 18,522 thousand). Such situation is attributed to the Group's exposure arising from the variable interest rates applied to long-term and short-term borrowings.

Credit Risk

Managing Accounts Receivable

Credit risk relates to the exposure inherent in the possibility that the contractual party fails to act upon its contractual commitments and cause the Group to suffer loss. The Group's exposure to this risk is limited to the amount of accounts receivable as of the balance sheet date. Accounts receivable are comprised of a large number of customers, where most significant portion is due from related parties.

The structure of accounts receivable as of December 31, 2011 is presented in the following table:

	<u>Gross Exposure</u>	<u>Allowance for Impairment</u>	<u>Net Exposure</u>
Accounts receivable, not matured	480,686	-	480,686
Accounts receivable matured and provided for	38,735	(38,735)	-
Accounts receivable matured, but not provided for	366,452	-	366,452
	<u>885,873</u>	<u>(38,735)</u>	<u>847,138</u>

The structure of accounts receivable as of December 31, 2010 is presented in the following table:

	<u>Gross Exposure</u>	<u>Allowance for Impairment</u>	<u>Net Exposure</u>
Accounts receivable, not matured	545,667	-	545,667
Accounts receivable matured and provided for	28,885	(28,885)	-
Accounts receivable matured, but not provided for	315,734	-	315,734
	<u>890,286</u>	<u>(28,885)</u>	<u>861,401</u>

Accounts Receivable not Matured

Accounts receivable, not matured as of December 31, 2011 in the amount of RSD 480,686 thousand (December 31, 2010: RSD 545,667 thousand) mostly refer to the receivables from the customers based on sales of services, maturing 60 to 90 days from the invoicing date, depending on the contractually-agreed terms. The average days sales outstanding in 2011 counted 75 days (2010: 76 days).

Accounts Receivable Matured and Provided for

In the period under review, the Group calculated an allowance for impairment of matured receivables in the amount of RSD 38,735 thousand (December 31, 2010: RSD 28,885 thousand), due from those customers whose creditworthiness has changed and which will not be collected in full.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

35. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)

Credit Risk (Continued)

Managing Accounts Receivable (Continued)

Accounts Receivable Matured but not Provided for

The Group did not make an allowance for impairment of receivables matured as of December 31, 2011 in the amount of RSD 366,452 thousand (December 31, 2010: RSD 315,734 thousand), according to the management's estimate based on collectability and the aging analysis of these receivables. The receivables are collectable in the period of three months, and accordingly, the Group did not form any allowance for impairment thereof.

Managing Accounts Payable

Accounts payable as of December 31, 2011 were stated in the amount of RSD 1,104,827 thousand (December 31, 2010: RSD 851,145 thousand), and are associated with the acquisition of services. These suppliers do not charge penalty against matured liabilities, whereas the Group duly settles accounts payable, as in accordance with financial risk management policies. The average days outstanding for accounts payable in 2011 counted 112 days (2010: 87 days).

Liquidity Risk

The ultimate responsibility for liquidity risk management resides with the Group's management, which is also responsible for managing the Group's short-term, medium-term and long-term financing and liquidity management. The Company manages liquidity by maintaining the necessary level of cash reserves, based on continued monitoring over the planned and actual cash flows, as well as by matching the maturities of financial assets and liabilities.

Tables of Liquidity and Credit Risk

The following tables give details of outstanding contractual maturities of assets of the Group. The amounts presented are based on the undiscounted cash flows arising from financial assets based on the earliest date upon which the Group will be able to collect such receivables.

Maturities of Financial Assets

	December 31, 2011					
	Less than One Month	From 1 to 3 Months	From 3 Months to 1 Year	From 1 to 5 Years	Over 5 Years	Total
Non-interest bearing	745,743	191,407	24,418	153	-	961,721
Fixed interest rate	187,095	-	-	-	43,270	230,365
	<u>932,838</u>	<u>191,407</u>	<u>24,418</u>	<u>153</u>	<u>43,270</u>	<u>1,192,086</u>
	December 31, 2010					
	Less than One Month	From 1 to 3 Months	From 3 Months to 1 Year	From 1 to 5 Years	Over 5 Years	Total
Non-interest bearing	732,962	290,472	34,686	153	-	1,058,273
Fixed interest rate	219,399	-	-	-	48,265	267,664
	<u>952,361</u>	<u>290,472</u>	<u>34,686</u>	<u>153</u>	<u>48,265</u>	<u>1,325,937</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2011

All amounts are expressed in thousands of RSD, unless otherwise stated.

35. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)

Liquidity Risk (Continued)

Tables of Liquidity and Credit Risk (Continued)

The following tables give details on outstanding contractual liabilities of the Company. The amounts presented are based on the undiscounted cash flows arising from financial liabilities based on the earliest date upon which the Company will be due to settle such payables.

Maturities of Financial Liabilities

	December 31, 2011					Total
	Less than One Month	From 1 to 3 Months	From 3 Months to 1 Year	From 1 to 5 Years	Over 5 Years	
Non-interest bearing	576,047	416,515	112,265	-	-	1,104,827
Fixed interest rate	613,744	605,178	569,820	376,483	-	2,165,225
Variable interest rate	206,309	146,759	703,297	1,118,279	-	2,174,644
	<u>1,396,100</u>	<u>1,168,452</u>	<u>1,385,382</u>	<u>1,494,762</u>	<u>-</u>	<u>5,444,696</u>

	December 31, 2010					Total
	Less than One Month	From 1 to 3 Months	From 3 Months to 1 Year	From 1 to 5 Years	Over 5 Years	
Non-interest bearing	559,435	268,109	23,601	-	-	851,145
Fixed interest rate	75,523	431,595	642,025	472,866	-	1,622,009
Variable interest rate	24,136	350,780	375,440	1,053,470	110,302	1,914,128
	<u>659,094</u>	<u>1,030,502</u>	<u>1,041,066</u>	<u>1,526,336</u>	<u>110,302</u>	<u>4,387,282</u>

Fair Value of Financial Instruments

The following table represents the present value of financial assets and liabilities and their fair value as of December 31, 2011 and 2010.

	December 31, 2011		December 31, 2010	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial Assets				
Long-term financial placements	41,720	41,720	45,468	45,468
Accounts receivable	847,138	847,138	861,401	861,401
Other receivables	45,820	45,820	41,761	41,761
Cash and cash equivalents	251,093	251,093	369,524	369,524
Short-term financial placements	4,765	4,765	4,986	4,986
	<u>1,190,536</u>	<u>1,190,536</u>	<u>1,323,140</u>	<u>1,323,140</u>
Financial Liabilities				
Long-term borrowings	1,270,109	1,270,109	1,729,282	1,729,282
Accounts payable	1,104,827	1,104,827	851,145	851,145
Current portion of long-term liabilities	761,386	761,386	520,358	520,358
Short-term financial liabilities	1,922,816	1,922,816	1,195,851	1,195,851
	<u>5,059,138</u>	<u>5,059,138</u>	<u>4,296,636</u>	<u>4,296,636</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***35. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)****Fair Value of Financial Instruments (Continued)***Assumptions for the Assessment of Financial Instruments' Fair Value*

Given that the sufficient market experience, stability and liquidity do not presently exist for the purchase and sale of financial assets or liabilities, and given that the quoted prices, which could be used for the purposes of disclosing fair value of financial assets and liabilities are unavailable, the method here applied is that of discounted cash flows. In using this method of measurement, interest rates for financial instruments with similar characteristics have been used, with the aim to arrive at the relevant assessment of market values of financial instruments as of the balance sheet date. The carrying value of short-term accounts receivable and accounts payable approximates their fair value since they fall due within relatively short periods.

37. OPERATING LEASE

Commitments of the Company based on cancellable contracts on the lease of business premises were the following:

	<u>December 31, 2011</u>	<u>December 31, 2010</u>
Up to 1 year	30,043	30,991
From 1 to 5 years	120,172	123,965
Over 5 years	-	30,991
	<u>150,215</u>	<u>185,947</u>

According to the lease contract, the rental of business premises expires at December 31, 2016.

38. CONTINGENT LIABILITIES

As of December 31, 2011, litigations filed against the Company and the Group sought an amount of RSD 832 thousand. Based on the analysis of available legal documents and information obtained from professional services and legal advisors, management believes that these legal matters will be resolved in favor of the Company and the Group, and accordingly, as of December 31, 2010, the financial statements do not include additional provisions for these risks.

The Group acts as a pledgor for a large number of short-term and long-term loans approved to its subsidiaries by domestic commercial banks. The total amount of such loans for which the Group may be liable at December 31, 2011 totaled RSD 1,083,628 thousand.

39. TAXATION RISKS

The Republic of Serbia tax legislation is subject to varying interpretations, and legislative changes occur frequently. The interpretation of tax legislation by tax authorities as applied to the transactions and activities of the Company may not concur with the views of the Company's management. Consequently, the relevant tax authorities may challenge transactions and the Company could be assessed additional taxes, penalties and interest, which can be significant. The fiscal periods remain open for review by the tax and customs' authorities with regard to the tax-paying entity's tax liabilities for a period of five years. This practically means that tax authorities can demand payment of outstanding liabilities in the period of five years from the origination of the liability.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**December 31, 2011***All amounts are expressed in thousands of RSD, unless otherwise stated.***40. EXCHANGE RATES**

The official exchange rates for major currencies determined in the interbank currency market and used in the translation of balance sheet components denominated in foreign currencies into dinars were as follows:

	<u>2011</u>	<u>2010</u>
USD	80,8662	79,2802
EUR	104,6409	105,4982
GBP	124,6002	122,4161
CHF	85,9121	84,4458