Tradition. Knowledge. Responsibility.

Consolidated Annual Report Končar D&ST Group

2018

KONČAR D&ST

ISO 9001:2015 / ISO 14001:2015 / OHSAS 18001:2007

Consolidated Annual Report Končar D&ST Group

2018

Končar D&ST Group

Velebit

Contents

I. MANAGEMENT BOARD REPORT ON THE KONČAR D&ST GROUP POSITION IN 2018

1. Introductory Word by the Management Board 5
2. Major 2018 Figures for the Group Compared to 2017 6
3. General Position of the Group 6
4. Group Organization and Management in 2018 7
5. Code of Corporate Governance 8
6. Market Position and Sales by Countries and Product Groups 9
7. Financial Position (Balance Sheet) 11
8. Operating Results (Income Statement) 11
9. Main Operating Risks for The Group 12
10. Investments and Technology Modernisation 13
11. Technical Development and Products Innovation 14
12. Human Resources 14
13. Quality Management, Environment Management and OH&S Management 15
14. Further Development Strategy 15

II. DECISIONS PROVIDED BY LAW

1. Decision on Approval of the Consolidated Annual Financial Statements for 2018 17

III. INDEPENDENT AUDITOR'S REPORT AND FINANCIAL STATEMENTS WITH NOTES

1. Responsibility for the Consolidated Annual Report 19
2. Independent Auditor's Report 20
3. Consolidated Financial Statements 26
   - Consolidated Statement of Comprehensive Income 26
   - Consolidated Statement of Financial Position 27
   - Consolidated Statement of Cash Flows 28
   - Consolidated Statement of Changes in Equity 29
4. Notes to the Consolidated Financial Statements 30

I

MANAGEMENT BOARD REPORT ON THE KONČAR D&ST GROUP POSITION IN 2018

Tradition. Knowledge. Responsibility.

1. Introductory Word by the Management Board

2018 - YEAR OF GROWTH AND PREPARATION FOR A STRATEGIC INVESTMENT

Končar D&ST Group consists of Končar D&ST d.d., Josipa Mokrovića 8, Zagreb, Croatia and Power Engineering Transformatory Sp. z o.o. (PET), Gdynska 83, Czerwonak, Poznan, Poland.

Total sales of goods and services of the Group in 2018 amounted to HRK 942 million (2017: HRK 907 million), which was a 4% increase on annual level. Export operations of HRK 788 million (2017: HRK 761 million) reached 84% of sales and exceeded by 4% the preceding year exports.

The 2018 profit before taxation was HRK 50.1 million (net: HRK 48.6 million) which was by 9% higher than in 2017, when it was HRK 45.9 million (net profit: HRK 44.4 million).

As a result of the IFRS 15 application in the Company's 2018 Financial Statements, its operating revenues grew by HRK 16.9 million and the profits grew by HRK 5.1 million.

Investment activities in 2018, mostly for purchase of new production, testing and IT equipment and improvement of working conditions in the production, amounted to HRK 11.8 million in Zagreb and HRK 7.1 million in PET Poland (in 2017: HRK 12.3 million was invested in equipment and HRK 22.3 million in the takeover of PET Poland). During the year, a strategic investment in the field of distribution transformer production was operatively managed and contracts were signed for the production hall and main production equipment.

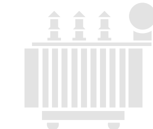
On 31 December 2018, the number of employees in the Group was 644, including 586 in Zagreb and 58 in PET Poland. The project of strengthening the technical and sales sector through inclusion of new highly educated employees continued. Parallel with the hiring, significant funds were invested in advanced software for product development and design as well as business management system.

The Group operates in alignment with the internationally recognized standards and social responsibility requirements.

Considering highly demanding conditions of the transformer market, the overall operating results of the Končar D&ST Group in 2018 were in our opinion successful and we believe the Group is well prepared for future challenges. Harmonized interests and mutual confidence among our shareholders, employees, partners and banks have been of great importance for such good performance. The Management of Končar D&ST d.d. is thankful for such support and trust and is pleased to present this Consolidated Annual Report for 2018.

For the Management Board of the Končar D&ST Inc.

Ivan Klapan
President of the Management Board



2. Major 2018 Figures for the Group Compared to 2017

	2018.	2017.	2018.	2017.	18/17
	HRK ('000)		EUR ('000)		index
Sales					
Croatia	154,879	146,363	20,890	19,619	105.8
Exports from Croatia	786,703	760,518	106,109	101,945	103.4
Total*	941,582	906,881	126,999	121,564	103.8
Net profit**	48,623	44,384	6,558	5,950	109.6
No. of employees					
as of 31/12	644	601			107.2

Note: Average exchange rate 2017: EUR 1 = HRK 7.4601
2018: EUR 1 = HRK 7.4141

* Total 2018 sales include the IFRS 15 effect of HRK 16.9 million.
**Net 2018 profit includes the IFRS 15 effect of HRK 5.1 million.

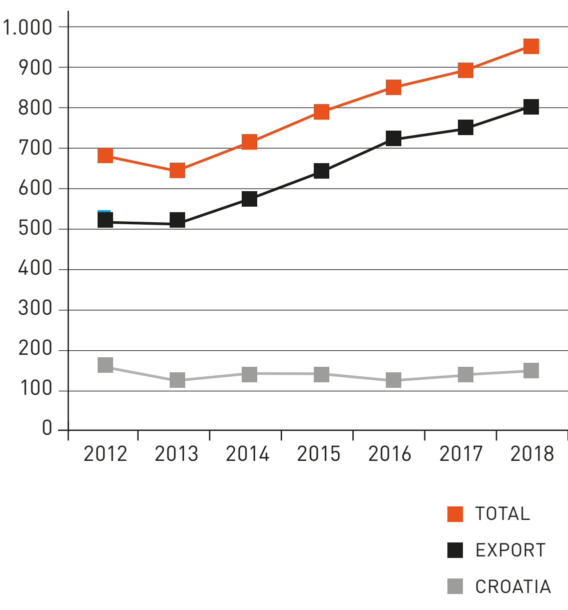
3. General position of the Group

Good operating results in 2018 have strengthened the Group's financial position and provided adequate financial stability and a good basis for further development.

Through the successful organizational adjustments to the high level of sales and production - both in the range of distribution transformers and that of medium power transformers - the Group has shown capacity to achieve its operating objectives in demanding environment and the strategic investment in the field of distribution transformers in Zagreb will strengthen its market position in the respective range.

Due to prioritizing of sales and development, as well as through recruitment and systematic onboarding of young experts, providing incentives to the employees, investments in product development and production modernisation, the Group is ready to face challenges of complex market conditions expected in future. Investment in Power Engineering Transformatory Sp. z o.o. (PET) Poland has opened another possibility of approaching new markets.

SALES TRENDS (HRK mil.)



4. Group Organisation and Management in 2018

Throughout 2018, Končar D&ST d.d. was managed by the Management Board consisting of the following members:

Ivan Klapan	President of the Management Board
Petar Bobek	Board Member, Business Development Director (since 01 April 2018)
Vanja Burul	Board Member, Director of the MPT Profit Centre
Martina Mikulić	Board Member, Director of the DT Profit Centre
Petar Vlaić	Board Member, Finance and Procurement Director

In 2018, the Končar D&ST d.d Supervisory Board members were:

Darinko Bago	President of the Supervisory Board
Miroslav Poljak	Vice President of the Supervisory Board
Jozo Miloloža	Supervisory Board member
Davor Mladina	Supervisory Board member
Vlado Grund	Supervisory Board member

PET Sp. z o.o. was managed by:

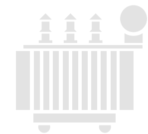
Lukasz Farulevski	Managing Director

Supervisory Board of PET Sp. z o.o

Ivan Klapan	President of the Supervisory Board
Miroslav Poljak	Vice President of the Supervisory Board
Petar Vlaić	Supervisory Board member
Waldemar Organista	Supervisory Board member
Grzegorz Kwiatkowski	Supervisory Board member (until 04 April 2018)
Natalia Mierzejewska	Supervisory Board member (since 04 April 2018)

Končar D&ST Group operated on two locations: Josipa Mokrovića 8, 10090 Zagreb, Croatia and Czerwonak, Gdinjska 83, Poland.

In order to manage the transport and assembly of medium power transformers in Morocco, there is a branch office in Casablanca, Morocco operating under the name Koncar D&ST Succursale Maroc.



5. Code of Corporate Governance

The parent-company of the Group is listed at the Zagreb Stock Exchange and applies the Code of Corporate Governance in accordance with the ZSE rules.

Končar D&ST d.d. implements most of the provisions of the Code of Corporate Governance, prepared by Zagreb Stock Exchange and Croatian financial services supervisory agency and released on the Zagreb Stock Exchange official website (www.zse.hr). Exceptions are certain provisions the Company finds non-applicable in the prescribed form, in particular:

- Supervisory Board and Audit Committee consist mostly of non-independent members, which is deemed appropriate in the current Company position within the Končar Group
- The Company has no long-term succession plan established but it does have a sufficient number of highly qualified, experienced and capable candidates within the Company for assuming all key positions where required
- There is no commission for appointments and rewards, but the appointment of new Management Board members and key management staff takes place in a well-organized manner and the rewarding policy is deemed adequate to the Company's position and its performance

The Company finds that the non-implementation of the respective Code provisions does not impair the high level of transparency of its operations and will not significantly affect investment decisions by either current or prospective investors.

A questionnaire with responses to 63 questions contains precise answers regarding the implemented and non-implemented provisions. The questionnaire is publicly available on the Zagreb Stock Exchange official website (www.zse.hr) and the Company's website (www.koncar-dst.hr).

Within its organizational model, in which the Company operates and in which all its business processes take place, the Company has developed internal control systems at all important levels. These systems, among other things, allow for an objective and fair presentation of the financial and business reports.

Information about significant shareholders is available on daily basis on the official Central Depository & Clearing Company website (www.skdd.hr), while its status on 31 December 2018 and 31 December 2017 was also published in the audit report. The shareholders are allowed the electronic voting with their attendance at General Assembly. Preferred shares of Končar D&ST do not provide any voting rights.

6. Market Position and Sales by Countries and Product Groups

Following the trends from the former years, the market in 2018 may in general be characterized as stable in demand with a further increase of supply. In addition to the constant pressure of the Asian producers in the Near East and Africa, their engagement on the European market has also intensified. Also, the market supply and demand in 2018 were also under impact of the trend of consolidations and changes in transformer manufacturer ownership structure that will in future lead to market changes depending on the new owners' policies.

The continuous engagement on the market, improvement of relations with customers and stakeholders, monitoring the product development trends and organizational changes aimed to improve the market position on the new markets has led to a stable growth in sales.

In 2018, the sales of goods and services grew by 3.8% from 2017 and, with the included IFRS 15 effect of HRK 16.9 million, amounted to HRK 941.6 million.

Per product groups, changes in 2018 compared to 2017 were:

- Distribution transformers: growth by 18.0 %
- Medium power transformers: decline by 0.9 %
- Dry and special transformers: decline by 17.4 %
- Other goods and services: decline by 0.4 %

Sales by major markets were as follows:

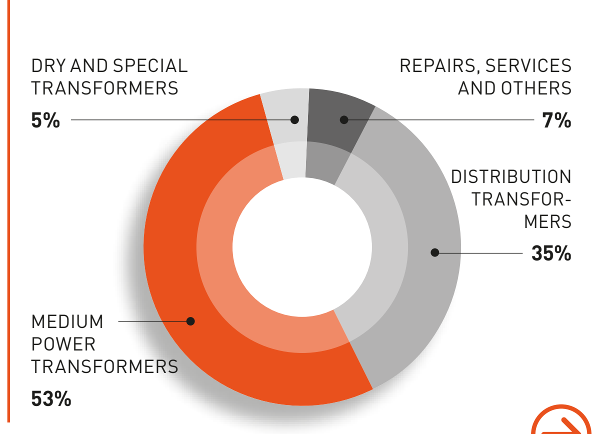
Croatia: the 2018 sales reached HRK 154.9 million which, compared to HRK 146.4 million in 2017, was a 5.8% growth.

Neighbouring European countries: Bosnia and Herzegovina, Slovenia, Macedonia, Montenegro, Austria, Italy, Czech Republic, Slovakia, Hungary, Kosovo, Serbia, Bulgaria, Romania, Albania - in 2018, the sales reached HRK 196.1 million which, compared to HRK 195 million in 2017, was a 0.6% growth.

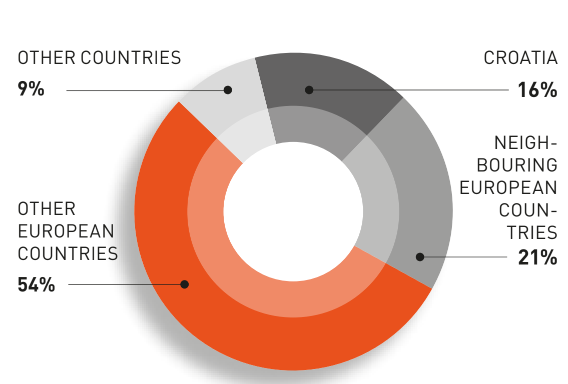
Other European countries: Sweden, Switzerland, Germany, Finland, Iceland, France, United Kingdom, Ireland, Poland, Estonia, Latvia, Lithuania, Cyprus, Spain, Denmark, Norway, Malta - deliveries in 2018 reached HRK 502.9 million which, compared to HRK 493.8 million in 2017, was an increase by 1.8%.

Other Asian, African and American countries: in 2018, deliveries worth HRK 87.7 million were made that, compared to HRK 63.2 million in 2017, constituted a growth by 38.7%.

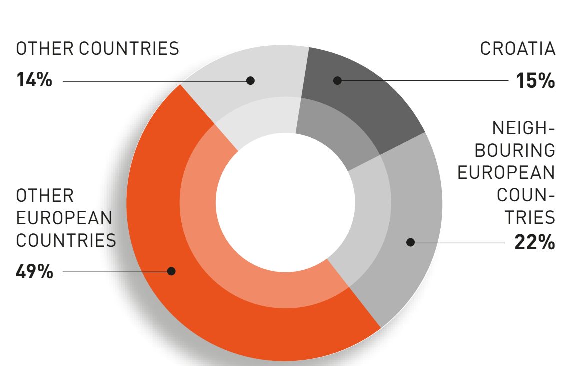
SALE STRUCTURE PER PRODUCTS (2018)



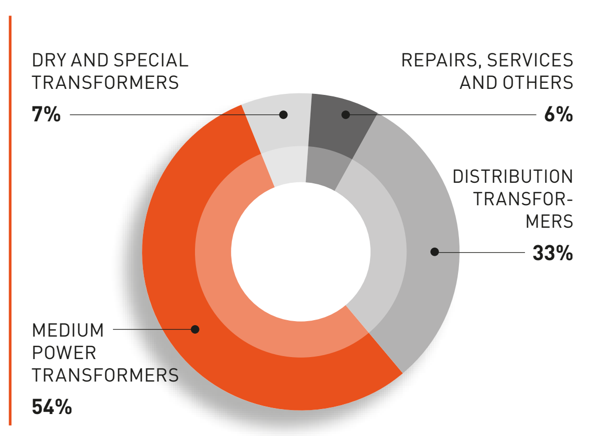
SALES STRUCTURE PER MARKETS (2018)



NEW CONTRACTS PER MARKETS (2018)



STRUCTURE OF NEW CONTRACTS PER PRODUCTS (2018)



7. Financial Position (Balance Sheet)

The Group's total assets on 31 December 2018 were HRK 765.7 million and their growth, compared to the balance on 31 December 2017, was HRK 98.2 million or 14.7%.

The share of fixed assets in the overall assets was 24% and their amount was HRK 183.1 million. The balance of fixed assets was higher by HRK 6.5 million than on the last day of the preceding year due to increased share of tangible assets in preparation.

Current assets in the amount of HRK 583 million formed 76% of the overall assets on 31 December 2018, which was by HRK 92 million or 19% higher than in the year before. The growth was mostly result of growth in two largest items of current assets, namely inventories and receivables from customers. Equity and reserves in the amount of HRK 328.2 million formed 43% of liabilities. Long-term provisions were HRK 112.3 million. Long-term liabilities on the balance sheet date were HRK 34.4 million and short-term liabilities amounted to HRK 215.4 million.

8. Operating Results (Income Statement)

In 2018, the Končar D&ST Group made HRK 954.8 million total revenues, which was by 3% more than in the year before. Revenues from sales were HRK 941.6 million and their structure consisted predominantly of the revenues made abroad in the amount of HRK 786.7 million or 84%. Total revenues from sales in Croatia were HRK 154.9 million.

On 01 January 2018, the International Financial Reporting Standard 15 (IFRS 15) - Revenues from Contracts with Customers took effect. Končar D&ST adopted the standard partially retroactively, with the implementation date as of 01 January 2018.

According to the Standard, some contracts recognized in 2017 based on the principle of recognition "over time" through the percentage of completion were again recognized for 2018. This led to increased revenues from sales in 2018 by HRK 16.9 million and higher profit before taxation by HRK 5.1 million. Profit after taxation was also higher by the same amount as the corporate income tax for the effects of these contracts had been paid in 2017.

In 2018, the consolidated profit before taxation was HRK 50.1 million which was by 9% higher than in 2017, when it was HRK 45.9 million. Consolidated profit after taxation in 2018 was HRK 48.6 million and exceeded by 10% the net 2017 profit of HRK 44.4 million.

Considering the HRK 5.1 million IFRS 15 effect on profit, profit before taxation without that effect would have been HRK 45 million and profit after taxation would have been HRK 43.5 million

In 2018, neither Končar D&ST as the parent company nor PET Poland as its subsidiary acquired any treasury shares.

9. Main Operating Risks for The Group

Market Risks. Demand for transformers on the target markets of the Group is one of the main operating risk factors. Global demand for transformers as well as demand on target markets varies significantly in specific periods, depending on a number of factors. Periods of high demand (positive trends) are definitely periods of easier contracting. On the other hand, periods of global recession and economic crisis bring more difficult contracting of new works and the resulting decrease in profit margins. **Supply** of transformers by other producers - competition pressure - is another significant risk factor for the Group operations. Transformer market is generally in most target export markets close to the full competition pattern or a form of mild oligopoly, and the market pressure on majority of the target markets is very strong. The entire transformer industry has been through major changes in the recent 10-20 years with a number of restructurings, winding-ups of plants, opening of new plants, take-overs and mergers (consolidations) and such trends will continue.

Procurement market risks. Prices of major raw materials and supplies for the production of transformers (copper, aluminium, transformer metal sheets, transformer oil, insulation, steel, etc.) have been volatile in the several recent years and sometimes with enormous growth or drop in a relatively short time period.
Considering the available options, the Group protects itself from the risk of sudden changes in prices of strategic raw materials in several ways. As for copper, being a raw material listed on commodity exchange markets (London Metal Exchange), forward contracts with the suppliers are used to agree on quantities and prices for the forward period based on the actual and forecast contracts. As for steel, transformer metal sheets and some important parts, their purchase is contracted with the suppliers on semi-annual or annual basis in order to reduce this risk. Also, in some several-year contracts with customers, the rolling formula is sometimes agreed based on change in the price in materials.

Currency risk is fairly expressed in the Group operations, considering a high percentage of exports and imports in its income and considering that majority of bank loans (both long-term and short-term ones) are expressed in EUR. The Group protects itself from currency risk by forward contracts with banks as well as by internal methods for harmonisation of currency inflow and outflow.

Technology and development risks. At this moment, the Group has at its disposal state-of-the-art technology for the transformer production and appropriate technical solutions for the majority of products within its range. The Group is capable of following technical and technological development at an enviable level. In future, technical and technological lag behind the major competitors is not expected.

Credit risk and liquidity risk. Credit risk is observed as a risk that a certain debtor of the Group (e.g. customer to whom the delivery was made without sufficient security) will not be able or willing to pay its dues to the Group in accordance with the agreed terms, and the Group will therefore incur losses by writing off or reducing such receivables.
Liquidity risk is expressed as a risk that the Group will not be able to fulfil the liabilities to its creditors in the agreed terms. The Group protects itself from credit risk with collaterals (L/C, guarantees, etc.), and evaluation of customer solvency in cooperation with external solvency and credit rating agencies. Also, certain trade receivables in respect of specific customers are secured at specialized institutions.
The Group has contracts with commercial banks about credit facilities which make possible to surmount its current need for liquid funds promptly and under well-known conditions. Also, receivables with relatively long maturity terms are most frequently collected by sale to financial institutions (factoring, forfaiting).

Management and personnel risk. Usual fluctuations and changes of management and leading experts do not have major effect on corporate operations while sudden or major fluctuations of such personnel could affect the corporate performance.

In addition to those specified above, there are also design risks, production risks, political risks and other risk groups present to a certain extent.

10. Investments And Technology Modernisation

The Group makes focused investments in the improvements and modernisation of processes that need to be raised to a higher technological level. Thus in 2018, the investment of HRK 11.8 million was made in the Zagreb site. Several specialized machines for the production were purchased or modernized - winding machines, transformer sheet processing machines, various specialized units, logistics and measuring equipment - in alignment with the adopted annual plan.

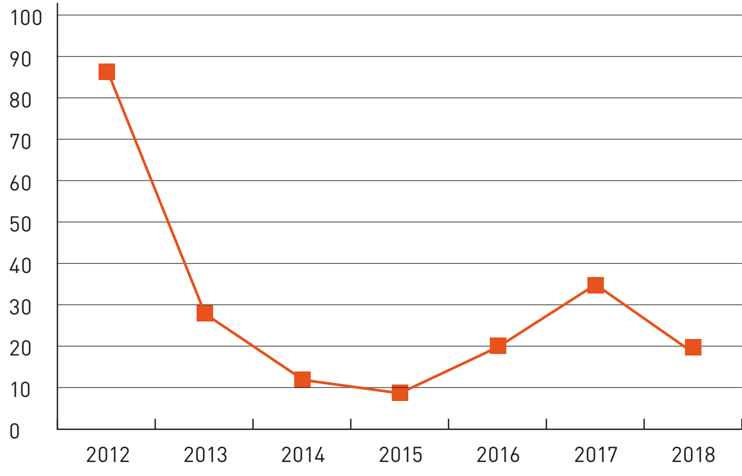
In 2018, Distribution Transformer Production Increase Project (DTPIP) was launched. The Project includes the expansion of production facilities and purchase of adequate quantity of required equipment. Through 2019, the project activities will intensify and the project completion is expected in the first half of 2020.

Parallel with the investment in the production equipment, investments were also made in ICT equipment development.

In PET Poland, the 2018 investments included HRK 7.1 million for procurement of new equipment, restructuring and modernisation of the factory and human resources. In addition to the financial investment, Končar D&ST d.d. invested its know-how and thereby supported further development and generation of a modern and competitive factory of medium power transformers in Poland with the expected mid-term return on investment.

Total 2018 investments of the Group were HRK 18.9 million.

INVESTMENT TRENDS (HRK mil.)



11. Technical Development and Product Innovation

In the field of medium power transformers in Končar D&ST d.d., dimensioning of cooling system with forced oil flow significantly improved in 2018. In cooperation with the Zagreb Electrical Engineering and Computing Faculty and the Zagreb Electrical Engineering Institute, efforts were made to reduce additional losses and to improve the expert base for loss calculation of power transformer load. A step forward was made also in the transformer insulation system, where optimization of technical and technology solutions yielded significant savings.

In PET Poland, the process of know-how transfer and implementation in business processes continued.

As for the distribution transformer range, the emphasis was on the improvement of expert base for noise through evaluation of the existing and the new transformer sheet types. Also, in cooperation with the Electrical Engineering Institute, the design and construction of the windings with graphite screens was revised. The new solution has accelerated the winding production process to a great extent without affecting the voltage conditions. As for special and large distribution transformers, the expert bases for no-load losses and the design software have been improved.

The cooperation continued with Končar Institute for Electrical Engineering, Zagreb Faculty of Electrical Engineering and Computing, Zagreb Faculty of Mechanical Engineering and Naval Architecture, and Poznan University of Technology in Poznan, Poland. There are several young professionals attending specialist and doctoral studies at the universities of Zagreb and Poznan.

Experts from the Technical Development and other departments actively participated in symposiums and seminars about transformers (CIGRE Paris, HO CIRED Opatija, Wetex Dubai, EuroTechCon Cardiff) and worked in the SO2 study committee for transformers and in the technical committees HZN/TO E14 Power Transformers and HZN/TO E10 Fluids for Use in Electrical Engineering.

12. Human Resources

On 31 December 2018, the number of employees in the Group was 644 (586 employees in Končar D&ST d.d. and 58 in PET Sp. z o.o.).

In the area of employee training, continuous training is conducted at universities and polytechnics studies. The Group supports enrolment in postgraduate studies, the result of which is a growing number of employees attending courses at various faculties. Promotion of professional and scientific training significantly enriches the know-how of the Group and its contacts with the relevant university institutions.

13. Quality Management, Environment Management and OH&S Management

Systematic quality management, environment management and occupational health and safety management in the Group is of exceptional importance as one of the operating elements to reach the set objectives.

In 2018, Končar D&ST d.d. conducted regular audits of all three certified management systems (ISO 9001:2015, ISO 14001:2015 and OHSAS 18001:2007).

In PET Poland, the audit of the certified quality management system under ISO 9001:2015 was also conducted. As for environment protection and OHS, the Company operates in compliance with the legal provisions and continues to promote environment protection, as well as health and safety of its employees and all visitors.

14. Further Development Strategy

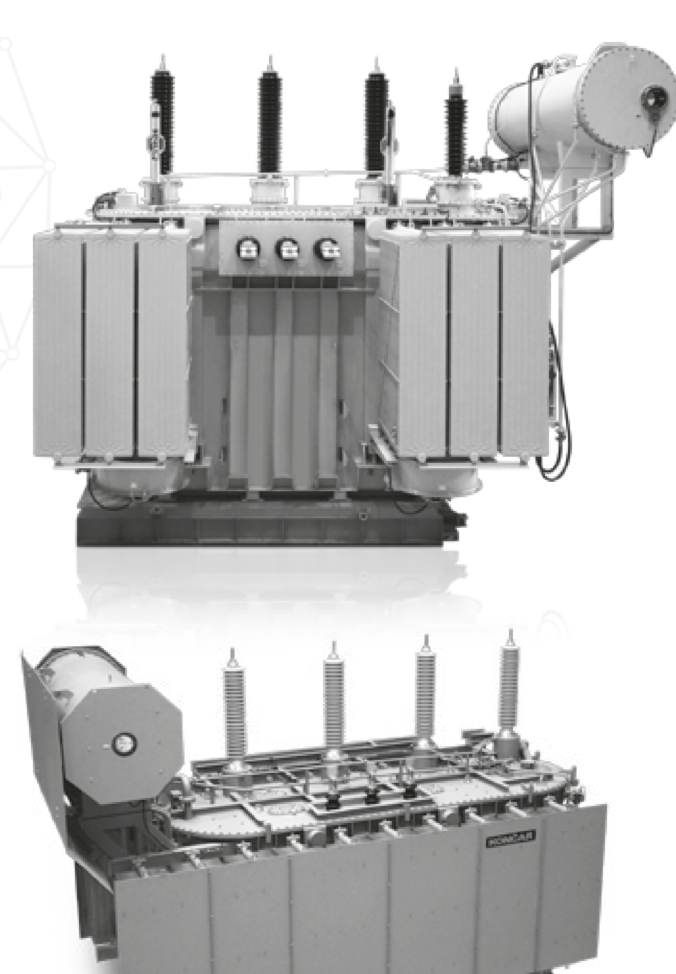
Development, sales and production of distribution oil transformers up to 8 MVA and 36 kV, special transformers, medium power transformers up to 100 MVA and 170 kV, as well as technology sales projects on selected markets will continue to be the core business activities of the Končar D&ST Group.

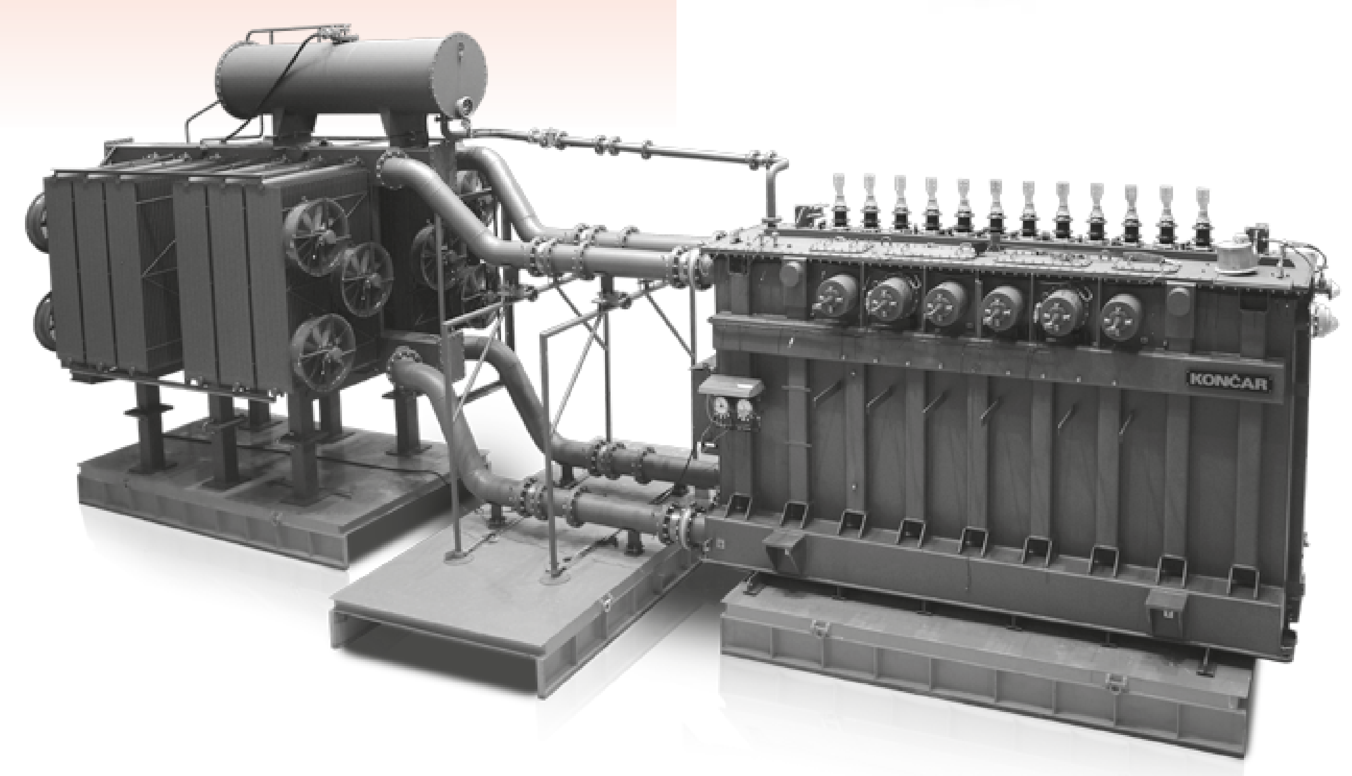
The Group will continue to secure its high position among the leading European manufacturers of distribution, special and medium power transformers through the recognition and best fulfilment of needs of its target customers, commitment to quality and sustainable development, technical and organisational development, as well as employee training and incentives aimed to the promotion of excellence and teamwork.

Final remark: From the end of 2018 until the preparation of this report, there have been no unusual or significant events that could significantly change the view of the operations and position of the Group as presented in this report.

II

DECISIONS PROVIDED BY LAW





Končar-Distribution and Special Transformers, Inc.
Zagreb, Josipa Mokrovića 8, PIN: 49214559889
(hereinafter: "the Company")

Pursuant to Articles 220 and 300d of the Croatian Act on Companies and Article 22 of the Articles of Association of KONČAR D&ST Inc., at the Supervisory Board meeting held on 26 March 2019, the Supervisory Board and the Management Board of the Company have adopted the following

DECISION
ON APPROVAL OF THE CONSOLIDATED
ANNUAL FINANCIAL STATEMENTS FOR 2018

The Supervisory Board and the Management Board of Končar-D&ST Inc. have jointly adopted the Consolidated Annual Financial Statements for 2018.

Explanation

The Management Board of the Company has submitted to the Supervisory Board for approval the Consolidated Financial Statements for 2018. The Supervisory Board has given approval to the Consolidated Financial Statements for 2018, whereby the Supervisory Board and the Management Board have jointly adopted the Consolidated Annual Financial Statements for 2018 as follows:

Total income	HRK	955,423,298
Total expenses	HRK	905,300,968
Profit before taxation	HRK	50,122,330
Corporate income tax	HRK	1,499,222
Profit after taxation	HRK	48,623,108
Total assets/liabilities	HRK	765,737,012

Darinko Bago
President of the Supervisory Board

Ivan Klapan
President of the Management Board

Zagreb, 26 March 2019

III
INDEPENDENT AUDITOR'S REPORT AND FINANCIAL STATEMENTS WITH NOTES
INFASURARI DE ALUMINIU

Responsibility for the Consolidated Annual Report

Pursuant to the Croatian Accounting Act, the Management Board is responsible for ensuring that consolidated financial statements are prepared for each financial year in accordance with International Financial Reporting Standards as adopted in the European Union which give a true and fair view of the consolidated financial position and consolidated financial performance of Končar - Distribution and Special Transformers Inc., Zagreb and its subsidiary (hereinafter: the Group) for that period.

The Management Board has a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. Therefore, the Management Board continues to adopt the going concern basis in preparing the consolidated financial statements.

In preparing consolidated financial statements, the responsibilities of the Management Board include ensuring that:

- suitable accounting policies are selected and then applied consistently;
- judgements and estimates are reasonable and prudent;
- applicable accounting standards are followed, subject to any material departures disclosed and explained in the consolidated financial statements; and
- consolidated financial statements are prepared on a going concern basis unless this assumption is inappropriate.

The Management Board is responsible for keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Group and their compliance with the Croatian Accounting Act. The Management Board is also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Moreover, in accordance with the Accounting Act, the Management Board is obliged to prepare a consolidated Annual Report comprising the consolidated financial statements, the consolidated Management Report and the Corporate Governance Statement. The consolidated Management Report was prepared in line with the requirements of Article 21 and 24 of the Accounting Act, and the Corporate Governance Statement in line with the requirements of Article 22 of the Accounting Act.

Ivan Klapan, President of the Management Board

Petar Vlaić, Member

Petar Bobek, Member

Martina Mikulić, Member

Vanja Burul, Member

Končar - Distribution and Special Transformers Inc.
Josipa Mokrovića 8
10 090 Zagreb
21 March 2019

Independent auditor's report to the Shareholders of Končar – Distribution and Special Transformers Inc.

Report on the audit of the consolidated financial statements

Our opinion

In our opinion, the accompanying consolidated financial statements give a true and fair view of the financial position of Končar – Distribution and Special Transformers Inc. (the "Company") and its subsidiaries (together – the "Group") as at 31 December 2018, and of their financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union ("IFRS").

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

What we have audited

The consolidated financial statements of the Group which comprise:

- The consolidated statement of comprehensive income for the year ended 31 December 2018;
- The consolidated statement of financial position as at 31 December 2018;
- The consolidated statement of cash flows for the year then ended;
- The consolidated statement of changes in equity for the year then ended; and
- The notes to the consolidated financial statements, which include significant accounting policies and other explanatory information.

Basis for opinion

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

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

Independence

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

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

The permitted non-audit services that we have provided to the Group, in the period from 1 January 2018 to 31 December 2018, are disclosed in Note 1 to the consolidated financial statements.

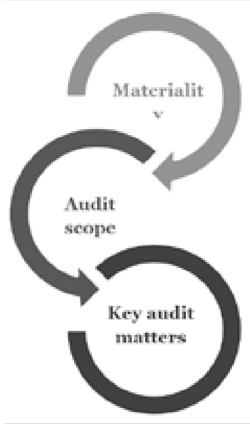
PricewaterhouseCoopers d.o.o., Heinzelova 70, 10000 Zagreb, Croatia
T: +385 (1) 6328 888, F:+385 (1) 6111 556, www.pwc.hr

Commercial Court in Zagreb, no. Tt-99/7257-2, Reg. No.: 080238978; Company ID No.: 81744835353; Founding capital: HRK 1,810,000.00, paid in full; Management Board: J. M. Gasparac, President; S. Dusic, Member; T. Macasovic, Member; Giro account: Raiffeisenbank Austria d.d., Petrinjska 59, Zagreb, IBAN: HR8124840081105514875.

Tradition. Knowledge. Responsibility.

Our audit approach

Overview



- Overall materiality for the financial statements of the Group as a whole: HRK 9,400 thousand, which is 1% of revenue

- Our audit scope addressed 97% of the Group's revenue and 86% of the Group's absolute value of underlying profit.

- Revenue recognition and adoption of IFRS 15

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

Materiality

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

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

Overall materiality for the financial statements as a whole	HRK 9,400 thousand
How we determined it	1% of revenue
Rationale for the materiality benchmark applied	We chose revenue as the key metric, because we consider it to be the benchmark which best reflects the Group's performance in the period under review. We selected 1%, which is within the range of commonly acceptable quantitative materiality thresholds in this sector.

Key audit matters

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

Key audit matters	How our audit addressed the Key audit matter
Revenue recognition and adoption of IFRS 15 *See Note 2B Revenue recognition, Note 3 Critical accounting estimates and Note 4 Revenue. In the consolidated statement of comprehensive income the Group reported revenue in the amount of HRK 941,582 thousand.* The adoption of the new standard for revenue recognition "International Financial Reporting Standard 15 – Revenue from Contracts with Customers" (IFRS 15) has a significant impact from 2018 going forward. In line with the transitional provisions, the Group applied the expedient allowing it to recognise the cumulative effect of transition at initial adoption of the standard directly in equity (within retained earnings) as at 1 January 2018. As a result, initial recognition of contract liabilities resulted in a decrease in retained earnings within equity of HRK 5,129 thousand as at 1 January 2018, as detailed in Note 2B. Given the complexity of the adoption of the new standard, the recognition and presentation of the impact of the IFRS 15 adoption was of particular importance for our audit.	Taking into account that management estimates and assumptions lead to an increased risk of misstatement, we have assessed the Group's revenue recognition processes and controls as part of our audit. Our audit approach included audit procedures comprising controls and substantive testing, which includes the following: • Obtaining an understanding of the process of sales and revenue recognition under IFRS 15 and the time control is transferred to the customer • Reviewing a sample of contracts, orders, invoices, delivery notes and other relevant documentation relating to the correct presentation of revenue under IFRS 15. We have satisfied ourselves as to the appropriateness of the existing systems, processes and controls and we have not identified any significant irregularities. Among other things, our audit approach included the following: • We have obtained a detailed overview of the calculation of the cumulative effect of applying the new standard on 1 January 2018 and verified its completeness and compliance with appropriate documentation in order to confirm the appropriateness of revenue recognition in the relevant period. • We have analysed samples of contracts with customers for all identified performance obligations and compared the Group's revenue recognition policy with the IFRS 15 requirements, taking into account the Group's operations. • We have assessed the accuracy and completeness of the presentation and disclosure of revenue and the effects of the first adoption of IFRS 15 on the Group's consolidated financial statements. Based on the obtained evidence, we have determined that the processes established by the Management Board and the assumptions used are sufficient and appropriate to ensure that the impact of the first-time adoption of IFRS 15 is recognised and disclosed correctly and that the revenue for 2018 is reported in accordance with the requirements of IFRS 15.

How we tailored our Group audit scope

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

Reporting on other information including the Management Report and Corporate Governance Statement

Management is responsible for the other information. The other information comprises the Annual Report of the Group, which includes the Management Report and Corporate Governance Statement, but does not include the consolidated financial statements and our independent auditor's report thereon.

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

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

With respect to the Management Report and Corporate Governance Statement, we also performed procedures required by the Accounting Act in Croatia. Those procedures include considering whether the Management Report includes the disclosures required by Article 21 and 24 of the Accounting Act, and whether the Corporate Governance Statement includes the information specified in Article 22 of the Accounting Act.

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

- the information given in the Management Report and the Corporate Governance Statement for the financial year for which the consolidated financial statements are prepared is consistent, in all material respects, with the consolidated financial statements;
- the Management Report has been prepared in accordance with the requirements of Article 21 and 24 of the Accounting Act, and
- the Corporate Governance Statement includes the information specified in Article 22 of the Accounting Act.

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

Responsibilities of management and those charged with governance for the consolidated financial statements

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

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

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

Auditor's responsibilities for the audit of the consolidated financial statements

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

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

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

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

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

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

Report on other legal and regulatory requirements

Appointment

We were first appointed as auditors of the Company on 23 May 2014. Our appointment has been renewed annually by shareholder resolution representing a total period of uninterrupted engagement appointment of 5 years.

The certified auditor engaged as partner on the audit resulting in this independent auditor's report is Kristina Dimitrov.

PricewaterhouseCoopers d.o.o.

PricewaterhouseCoopers d.o.o.
Heinzelova 70, Zagreb
21 March 2019

Consolidated Statement of Comprehensive Income

for the Year Ended 31 December 2018

	Note	2018	2017
		HRK	*HRK*
Revenue	4	941,582,401	906,880,947
Other operating income	5	1,053,437	2,236,005
Operating income		**942,635,838**	**909,116,952**
Increase/(decrease) in inventories of work in progress and finished goods		27,196,270	(22,914,105)
Cost of materials and energy	6	(624,292,688)	(544,284,973)
Cost of goods sold		(30,709,501)	(30,880,077)
Service costs	7	(76,956,000)	(77,186,664)
Staff costs	8	(137,857,964)	(127,930,496)
Depreciation and amortisation	9	(19,277,140)	(19,617,469)
Other expenses	10	(25,333,415)	(23,732,493)
Impairment	11	(2,105,516)	(6,349,804)
Impairment of financial assets		(115,966)	(49,616)
Provisions	12	(3,612,210)	(21,025,445)
Other operating expenses		(1,461,435)	(671,139)
Operating expenses		**(894,525,565)**	**(874,642,281)**
Operating profit		**48,110,273**	**34,474,671**
Gain on bargain purchase	41	**-**	**8,903,103**
Finance income	13	12,194,242	12,445,652
Finance costs	14	(10,775,403)	(10,193,944)
Net finance result		**1,418,839**	**2,251,708**
Total income		**954,830,080**	**930,465,707**
Total expenses		**(905,300,968)**	**(884,836,225)**
Share in profit of investments accounted for using the equity method	15	593,218	284,500
Profit before tax		**50,122,330**	**45,913,982**
Income tax	16	(1,499,222)	(1,550,578)
PROFIT FOR THE YEAR		**48,623,108**	**44,363,404**
Other comprehensive income			
Exchange differences on translation of foreign operations		(668,540)	245,487
Other comprehensive income/(loss)		**(668,540)**	**245,487**
COMPREHENSIVE INCOME FOR THE YEAR		**47,954,568**	**44,608,891**
Profit for the period attributable to:			
Owners of the Company		48,623,108	44,363,404
Non-controlling interest		-	-
Comprehensive income attributable to:			
Owners of the Company		47,954,568	44,608,891
Non-controlling interest		-	-
Earnings per share (basic and diluted) in HRK	17	**95.11**	**86.78**

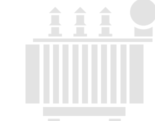
The accompanying notes form an integral part of these financial statements.

Consolidated Statement of Financial Position

as at 31 December 2018

	Note	31 December 2018	31 December 2017
		HRK	*HRK*
ASSETS			
Non-current assets			
Intangible assets	18	2,651,830	2,396,559
Property, plant and equipment	19	168,536,805	163,121,053
Investment property	20	3,339,582	3,500,000
Investments accounted for using the equity method	21	4,821,718	4,368,500
Financial assets	22	2,838,665	2,862,110
Receivables		659,606	-
Deferred tax assets	16	231,150	264,224
		183,079,356	**176,512,446**
Current assets			
Inventories	23	264,066,649	200,445,554
Receivables from related parties	24	17,931,894	42,906,848
Trade receivables	25	183,102,787	113,415,938
Contract assets	26	8,160,665	-
Other receivables	27	4,765,582	2,732,851
Financial assets	28	293,340	882,706
Cash and cash equivalents	29	103,777,825	130,043,399
Prepaid expenses		558,914	588,460
		582,657,656	**491,015,756**
TOTAL ASSETS		**765,737,012**	**667,528,202**
EQUITY AND LIABILITIES			
Share capital	30	**153,369,600**	**76,684,800**
Legal reserves	30	3,839,641	3,839,641
Statutory reserves	30	76,684,800	153,369,600
Other reserves	30	45,982,991	25,231,495
Translation reserves		(423,053)	245,487
Retained earnings		**87,517**	**2,551,542**
Profit for the year		**48,623,108**	**44,363,404**
EQUITY		**328,164,604**	**306,285,969**
Warranty provisions		96,668,060	99,624,792
Provisions for pensions, termination benefits and similar liabilities		15,608,997	15,224,434
Provisions	31	**112,277,057**	**114,849,226**
Liabilities from purchase of shares	32	8,131,049	8,001,769
Liabilities to banks (borrowings) and financial institutions	33	26,228,233	36,895,965
Non-current liabilities		**34,359,282**	**44,897,734**
Liabilities to related parties	34	8,233,655	6,696,470
Liabilities to banks (borrowings) and financial institutions	35	19,427,829	9,614,576
Trade payables	36	102,822,474	69,350,738
Contract liabilities		84,970,726	
Advances received	26	-	45,943,641
Other liabilities	37	18,033,513	16,061,778
Accrued expenses and deferred income	38	2,077,684	4,592,845
Current provisions	39	55,370,188	49,235,225
Current liabilities		**290,936,069**	**201,495,273**
Total liabilities		**437,572,408**	**361,242,233**
TOTAL EQUITY AND LIABILITIES		**765,737,012**	**667,528,202**

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



Consolidated Statement of Cash Flows

for the Year Ended 31 December 2018

	Note	2018	2017
		HRK	*HRK*
Cash flows from operating activities			
Cash proceeds from trade receivables		920,912,862	868,954,831
Cash proceeds from insurance reimbursements		65,874	15,797
Cash proceeds from tax returns		45,340,663	43,096,205
Cash paid to suppliers		(773,144,278)	(678,686,691)
Cash paid to employees		(130,231,961)	(121,409,235)
Taxes paid		(26,983,052)	(21,379,893)
Cash paid for insurance related to reimbursements		(2,117,528)	(1,648,753)
Other cash proceeds and payments		(14,748,404)	(16,186,723)
Cash from operations		**19,094,176**	**72,755,538**
Interest paid		(733,209)	(1,066,257)
Net cash flows from operating activities		**18,360,967**	**71,689,281**
Cash flows from investing activities			
Proceeds from sale of non-current tangible and intangible assets		446,609	338,798
Dividends received		1,423,404	2,113,086
Interest received		28,560	33,315
Purchase of non-current tangible and intangible assets		(23,596,726)	(14,946,000)
Net cash used in investing activities		**(21,698,153)**	**(12,460,801)**
Cash flows from financing activities			
Proceeds from borrowings	33, 35	8,483,832	23,352,783
Repayment of borrowings	35	(8,340,195)	(9,017,784)
Dividends paid	30	(20,756,975)	(14,373,288)
Finance lease payments	35	(564,810)	(597,135)
Other cash proceeds and payments		(1,750,240)	(428)
Net cash used in financing activities		**(22,928,388)**	**(635,852)**
Net (decrease)/increase in cash and cash equivalents		**(26,265,574)**	**58,592,628**
Cash and cash equivalents at the beginning of the year		130,043,399	71,450,771
Cash and cash equivalents at the end of the year	29	**103,777,825**	**130,043,399**

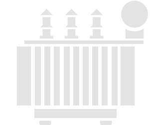
The accompanying notes form an integral part of these financial statements.

Consolidated Statement of Changes in Equity

for the Year Ended 31 December 2018

	Share capital	**Legal reserves**	**Statutory reserves**	**Other reserves**	**Trans-lation reserves**	**Retained earnings**	**Profit for the year**	**Total equity**
	HRK	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*
At 1 January 2017	**76,684,800**	**3,839,641**	**145,672,503**	**11,371,723**	**-**	**2,441,630**	**36,040,069**	**276,050,366**
Profit for the year	-	-	-	-	-	-	44,363,404	**44,363,404**
Other comprehensive income:								
Exchange differences on translation of foreign operations	-	-	-	-	245,487	-	-	245,487
Total comprehensive income	**-**	**-**	**-**	**-**	**245,487**	**-**	**44,363,404**	**44,608,891**
Transactions with owners:								
Transfer to reserves	-	-	7,697,097	13,859,772	-	109,912	(21,666,781)	-
Dividends paid	-	-	-	-	-	-	(14,373,288)	**(14,373,288)**
	-	-	*7,697,097*	*13,859,772*	-	*109,912*	*(36,040,069)*	**(14,373,288)**
At 31 December 2017	**76,684,800**	**3,839,641**	**153,369,600**	**25,231,495**	**245,487**	**2,551,542**	**44,363,404**	**306,285,969**
Effects of the adoption of new standards (Note 2B)	-	-	-	-	-	*(5,128,643)*	-	**(5,128,643)**
At 1 January 2018	**76,684,800**	**3,839,641**	**153,369,600**	**25,231,495**	**245,487**	**(2,577,101)**	**44,363,404**	**301,157,326**
Profit for the year	-	-	-	-	-	-	48,623,108	**48,623,108**
Other comprehensive income								
Exchange differences on translation of foreign operations	-	-	-	-	(668,540)	-		(668,540)
Total comprehensive income	**-**	**-**	**-**	**-**	**(668,540)**	**-**	**48,623,108**	**47,954,568**
Conversion of reserves into share capital	76,684,800	-	(76,684,800)	-	-	-	-	-
Transakcije sa vlasnicima:								
Transfer to reserves	-	-	-	20,751,496	-	2,664,618	(23,607,385)	**(191,271)**
Dividends paid	-	-	-	-	-		(20,756,019)	**(20,756,019)**
	76,684,800	-	*(76,684,800)*	*20,751,496*	-	*2,664,618*	*(44,363,404)*	**(20,947,290)**
At 31 December 2018	**153,369,600**	**3,839,641**	**76,684,800**	**45,982,991**	**(423,053)**	**87,517**	**48,623,108**	**328,164,604**

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



Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

1. General information on the Group

The principal activities of the Končar Group - Distribution and Special Transformers Inc. are the design, production, placement and servicing of distribution, special and medium power transformers up to 100 MVA and voltage up to 170 kV.

The Group consists of the parent company Končar - Distribution and Special Transformers Inc. and the subsidiary Power Engineering Transformatory Sp. z.o.o. On 8 May 2017, a contract was signed on the acquisition of the majority ownership share (74% share) in Power Engineering Transformatory Sp. z o.o. (PET) from Czerwonak, Poznan, Poland. The principal activity of the stated company is the design, production, placement and servicing of medium power transformers up to 63 MVA and voltage up to 145 kV. The consideration paid for the acquisition of the 74% share will be used to purchase new equipment and modernise the factory.

Shares in ownership and voting rights as at 31 December were as follows:

	31 December 2018		31 December 2017	
	Ownership share (%)	*Voting rights share (%)*	*Ownership share (%)*	*Voting rights share (%)*
Power Engineering Transformatory (PET)	74	74	74	74

The Company also has the associate Elkakon Ltd. with an ownership share of 50%.

As at 31 December 2018, the Group had 644 employees, while as at 31 December 2017 the Group had 601 employees.

The Group has a subsidiary in Morocco (which is not a legal entity), and its financial information is included in the Group's financial statements.

The employee structure is as follows:

	31 December 2018	31 December 2017
University degree, Master's degree and PhD	238	213
College	25	27
Secondary school qualifications	311	281
Skilled workers	44	49
Primary school + training on the job	26	31
Total	**644**	**601**

Members of the Supervisory Board

- Darinko Bago, President
- Miroslav Poljak, Deputy
- Jozo Miloloža, Member
- Davor Mladina, Member
- Vlado Grund, Member

Members of the Management Board

- Ivan Klapan, President
- Petar Vlaić, Member
- Martina Mikulić, Member
- Vanja Burul, Member
- Ivan Sitar, ceased to be a member as of 2 January 2018
- Petar Bobek, Member as of 1 April 2018

Compensations paid to members of the Management Board and Supervisory Board of the Group are disclosed in Notes 8 and 10 to the financial statements.

In 2018, non-audit services provided to the Group amounted to HRK 29,722 net (2017: HRK 27,180).

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

2. Summary of significant accounting policies

The significant accounting policies used for the preparation of these financial statements are presented below. These accounting policies have been consistently applied to all the years presented, unless otherwise stated.

Basis of preparation

The Group's consolidated financial statements have been prepared in accordance with the applicable laws in the Republic of Croatia and International Financial Reporting Standards adopted in the European Union.

The consolidated financial statements have been prepared using the historical cost convention, except for available-for-sale financial assets, financial assets and liabilities at fair value through profit or loss and liabilities which are stated at fair value. The consolidated financial statements have been prepared under the accrual principle on a going concern basis.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires the Management Board to exercise its judgement in the process of applying the Group's accounting policies. The areas where assumptions and estimates are significant to the financial statements are disclosed in Note 3.

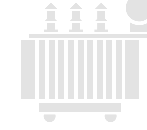
The Group's financial statements are presented in Croatian kuna as the functional and presentation currency of the Group. As at 31 December 2018, the exchange rate for EUR 1 and USD 1 was HRK 7.42 and HRK 6.47 (31 December 2017: HRK 7.51 and HRK 6.27). All amounts disclosed in these consolidated financial statements are expressed in HRK unless otherwise stated.

New and amended standards adopted and effective

The Group has adopted the following new and amended IFRS, interpretations and improvements for its annual reporting period commencing 1 January 2018 which were endorsed by the European Union and which are relevant for the Group's financial statements:

- IFRS 15 Revenue from Contracts with Customers and associated amendments to various other standards
- Amendments to IFRS 15 Revenue from Contracts with Customers
- IFRS 9 Financial instruments and associated amendments to various other standards
- Amendments to IAS 40 - Transfers of Investment Property
- IFRIC 22 - Foreign Currency Transactions and Advance Consideration
- Amendments to IFRS 2 Classification and Measurement od Share-based Payment Transactions
- Annual Improvements to 2014-2016 Reporting Cycle
  - IAS 28 Investments in Associates and Joint Ventures
  - IFRS 1 First-time Adoption of International Financial Reporting Standards

The Group adopted IFRS 15 and IFRS 9 for the first time as of 1 January 2018. The nature and effects of changes resulting from the adoption of new standards are set detailed in item A.



Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

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

Standards, interpretations and amendments issued but not yet effective

Certain new standards and amendments to IFRS and IFRIC guidance have been issued that are not effective for the reporting periods ending 31 December 2018 and which the Group has not early adopted. None of these is expected to have a significant effect on the Group's financial statements, except for the following standards:

IFRS 16 Leases (issued in January 2016 and effective for annual periods beginning on or after 1 January 2019)

- IFRS 16 will affect primarily lessee accounting and will result in the recognition of almost all leases on the balance sheet. The standard removes the current distinction between operating and financing leases and requires recognition of an asset (the right to use the leased item) and a financial liability to pay rentals for virtually all lease contracts. An optional exemption exists for short-term and low-value leases.
- The income statement will also be affected because the total expense is typically higher in the earlier years of a lease and lower in later years. Additionally, operating expense will be replaced with interest and depreciation, so key metrics like EBITDA will change.
- Operating cash flows will be higher as cash payments for the principal portion of the lease liability are classified within financing activities. Only the part of the payments that reflects interest can continue to be presented as operating cash flows.
- Lessor accounting will not change significantly. Some differences may arise as a result of the new guidance on the definition of a lease. Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

The standard will affect primarily the accounting for the Group's operating leases. During 2018, the Group has made a preliminary assessment and calculation of effects of applying IFRS 16 as of 1 January 2019 for operating lease contracts and the application of new rules would result in the disclosure of right-of-use assets in the amount of HRK 823 thousand and lease liabilities in the amount of HRK 823 thousand.

The Group plans to adopt this standard on its effective date. The Group intends to apply the simplified transition approach and will not restate comparative amounts for the year prior to first adoption. Right-of-use assets for property leases are measured on transition as if the new rules had always applied. All other right-of-use assets are measured at the amount of the lease liability on adoption (adjusted for any prepaid or accrued lease expenses).

IFRIC 23 - Uncertainty over Income Tax Treatments was issued in June 2016 and is effective for annual periods beginning on or after 1 January 2019.

The following is considered in particular:

- how to determine the appropriate accounting unit and that each uncertain income tax treatment should be determined separately or together as a group, based on which approach better predicts the resolution of the uncertainty.
- an entity should assume that a taxation authority will examine the uncertain tax treatments and obtain all related information, i.e. it should disregard the risk of detection

- an entity should reflect the effect of uncertainty in determining the income tax when it is not probable that the tax authority will accept the tax treatment
- the effect of uncertainty should be measured by using either the most likely amount or expected value, whidepending on which method better predicts the resolution of the uncertainty, and
- the judgements or estimates must be reassessed whenever the circumstances change or new information is available that affects the judgements.

Although there are no new disclosure requirements, entities are reminded of the general requirement to provide information on judgments and estimates when preparing financial statements.

The Management Board estimates that the adoption of the amendments will not have a material effect on the Group's financial statements and plans to adopt the amendments on their effective date.

Standards, interpretations and amendments issued by the IASB, which have not been adopted by the EU:

Amendments to IAS 28 - Long-term interests in Associates and Joint Ventures (effective for annual periods beginning on or after 1 January 2019 - IASB)

The amendments clarify the accounting treatment of long-term investments in associates or joint ventures, that form part of a net investment in an associates or a joint venture, but to which the equity method does not apply. Before applying the loss allocation requirement and impairment losses from AASB 128 Investments in associates and joint ventures, entities must account for such investments in accordance with AASB 9 Financial Instruments.

The Management does not expect the adoption of the amendments to have a material impact on the Group's financial statements and plans to adopt the amendments as of their effective date.

Annual improvements to 2015 - 2017 Cycle were issued in December 2017 and are effective for annual periods beginning on or after 1 January 2019, and they include clarifications to the following standards:

- IFRS 3 Business Combinations - clarifies that obtaining control of a business that is a joint operation is a business combination achieved in stages.
- IFRS 11 - Joint Arrangements - clarifies that the party obtaining joint control of a business that is a joint operation should not remeasure its previously held interest in the joint operation.
- IAS 12 - Income Taxes - clarifies that the tax consequences of dividends on financial instruments classified as equity should be recognised depending on where the entity recognises the past transactions or events that generated distributable profits.
- IAS 23 Borrowing Costs - clarifies that if any specific borrowing remains outstanding after the related qualifying asset is ready for its intended use or sale, that borrowing becomes part of the general borrowings.

The Group will apply the amendments on their effective date.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Amendments to IFRS 10 and IAS 28 - Sale or Contribution of Assets between an Investor and its Associate or Joint Venture - In December, the IASB decided to defer the application date of this amendment until such time as the IASB has finalised its research project on the equity method.

The amendments clarify the accounting treatment for sales or contribution of assets between an investor and its associates or joint ventures. They confirm that the accounting treatment depends on whether the non-monetary assets sold or contributed to an associate or joint venture constitute a 'business' (as defined in IFRS 3 Business Combinations).

Where the non-monetary assets constitute a business, the investor will recognise the full gain or loss on the sale or contribution of assets. However, any gain or loss (as a result of a sale or non-operational asset) is recognised only to the amount invested by another investor in an associate or a joint venture. The amendments apply prospectively. The Management Board estimates that the adoption of the improvements will not have a material effect on the financial statements of the Company and plans to adopt the standard on its effective date and when endorsed by the European Union.

Amendments to IFRS 3 Business Combinations - issued on 22 October 2018 acquisitions from the beginning of annual reporting period that starts on or after 1 January 2020.

The amendments revise the definition of a business. A business must have inputs and a substantive process that together significantly contribute to the ability to create outputs. The new guidance provides a framework to evaluate when an input and a substantive process are present, including for early stage companies that have not generated outputs. An organised workforce should be present as a condition for classification as a business if are no outputs. The definition of the term 'outputs' is narrowed to focus on goods and services provided to customers, generating investment income and other income, and it excludes returns in the form of lower costs and other economic benefits. It is also no longer necessary to assess whether market participants are capable of replacing missing elements or integrating the acquired activities and assets. An entity can apply a 'concentration test'. The assets acquired would not represent a business if substantially all of the fair value of gross assets acquired is concentrated in a single asset (or a group of similar assets).

Amendments to IAS 1 and IAS 8: Definition of materiality - issued on 31 October 2018 and effective for annual periods beginning on or after 1 January 2020.

The amendments clarify the definition of materiality and how it should be applied by including in the definition guidance that until now has featured elsewhere in IFRS. In addition, the explanations accompanying the definition have been improved. Finally, the amendments ensure that the definition of material is consistent across all IFRS Standards. Information is material if omitting, misstating or obscuring it could reasonably be expected to influence the decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.

Amendments to the Conceptual Framework for Financial Reporting - issued on 29 March 2018 and effective for annual periods beginning on or after 1 January 2020.

The revised Conceptual Framework includes a new chapter on measurement; guidance on reporting financial performance; improved definitions and guidance - in particular the definition of a liability; and clarifications in important areas, such as the roles of stewardship, prudence and measurement uncertainty in financial reporting.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

a) Basis for consolidation

The consolidated financial statements of the Group include the financial statements of the Parent company and the financial statements of the companies controlled by the Parent company (subsidiaries). The Group controls an entity when the group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the group. They are deconsolidated from the date that control ceases.

All inter-group transactions, balances and unrealised gains on transactions among the Group companies are eliminated. Unrealised losses are also eliminated. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

Changes in ownership interests in subsidiaries without change of control

The Group applies a policy of treating transactions with non-controlling interests that do not result in loss of control as equity transactions - that is, as transactions with the owners in their capacity as owners. For purchases from minority shareholders, the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

Disposal of subsidiaries/loss of control over subsidiaries

When the Group ceases to have control, any retained interest in the entity is remeasured to its fair value at the date when control is lost, with the change in carrying amount recognised in profit or loss. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognised in other comprehensive income in respect of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities. This may mean that amounts previously recognised in other comprehensive income are reclassified to the income statement.

b) Investments in associates

Associated companies are companies in which the Group has between 20% and 50% of voting power and in which the Group has significant influence, but not control. In the consolidated financial statements investments in associates are accounted for using the equity method of accounting. Under the equity method, the investment is initially recognised at cost, and the carrying amount is increased or decreased to recognise the investor's share of the profit or loss of the investee after the date of acquisition. The Group's investment in associates includes goodwill identified on acquisition. Dividends received or receivable from associates are deducted from the carrying value of the investment.

If the ownership interest in an associate is reduced but significant influence is retained, only a proportionate share of the amounts previously recognised in other comprehensive income is reclassified to profit or loss where appropriate.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

The Group's share of post-acquisition profit or loss is recognised in the income statement, and its share of post-acquisition movements in other comprehensive income is recognised in other comprehensive income with a corresponding adjustment to the carrying amount of the investment. When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred legal or constructive obligations or made payments on behalf of the associate.

The Group determines at each reporting date whether there is any objective evidence that the investment in the associate is impaired. If this is the case, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognises the amount adjacent to 'share of profit/(loss) of associates' in the income statement.

Profits and losses resulting from upstream and downstream transactions between the group and its associate are recognised in the group's financial statements only to the extent of unrelated investor's interests in the associates. Unrealised losses are eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group. Dilution gains and losses arising in investments in associates are recognised in the income statement.

c) Business combinations

Business combinations are accounted for by applying the acquisition method. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The Group recognises any non-controlling interest in the acquiree at the non-controlling interest's proportionate share of the recognised amounts of acquiree's identifiable net assets. Acquisition-related costs are expensed as incurred.

d) Goodwill

Goodwill arises on the acquisition of subsidiaries and represents the excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquire over the fair value of the identifiable net assets acquired.

If the total of consideration transferred, non-controlling interest recognised and previously held interest measured at fair value is less than the fair value of the net assets of the subsidiary acquired, in the case of a bargain purchase, the difference is recognised directly in the income statement.

For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the Group's CGUs, or groups of CGUs, that are expected to benefit from the synergies of the combination. Each unit or group of units to which the goodwill is allocated represents the lowest level within the Group at which the goodwill is monitored for internal management purposes. Goodwill is monitored at the operating segment level.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Goodwill impairment reviews are undertaken annually or more frequently if events or changes in circumstances indicate a potential impairment. The carrying value of the CGU containing the goodwill is compared to the recoverable amount, which is the higher of value in use and the fair value less costs of disposal.

Any impairment is recognised immediately as an expense and is not subsequently reversed.

e) Finance income and costs

Finance income and costs comprise the interest accrued on loans and borrowings calculated using the effective interest method, receivables for interest on investments, dividend income, foreign exchange gains and losses, gains and losses from financial assets at fair value through profit or loss.

Interest income is recognised in the income statement on an accrual basis using the effective interest rate method. Dividend income or income from share in profit is recognised in the income statement at the date when the Group's right to receive payment is established.

Finance costs comprise interest on loans, changes in fair value of financial assets at fair value through profit or loss, impairment losses from financial assets and foreign exchange losses.

f) Borrowing costs

Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are capitalised during the period indispensable for the finalisation and preparation of the asset for its intended use or sale. Other borrowing costs are recognised in profit or loss using the effective interest method.

g) Taxes

The parent company accounts for for taxes in accordance with Croatian law. Income tax for the year comprises current and deferred tax.

Current tax is the expected tax payable on the taxable income for the year, using tax rates in effect at the balance sheet date.

Deferred taxes arise from temporary differences between the amounts of assets and liabilities in the financial statements and the values presented for the purposes of determining the income tax base. A deferred tax asset for unused tax losses and unused tax benefits is recognised to the extent that it is probable that future taxable profit will be realised on the basis of which the deferred tax assets will be utilised. Deferred tax assets and liabilities are calculated using the tax rate applicable to the taxable profit in the years in which these assets or liabilities will be realised.

Current and deferred tax are recognised as income or expense in the income statement; except when they relate to items credited or debited in other comprehensive income or directly in equity, in which case tax is also recognised in other comprehensive income or directly in equity.

h) Segment information

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

maker. The chief operating decision maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Management/Supervisory Board that makes strategic decisions.

The Group's Management Board monitors its operations as a single operating segment, while only sales revenues are monitored as two operating segments: Medium power transformers and Distribution transformers as presented in Note 4.

i) Earnings per share

The Group presents basic and diluted earnings per share data for its ordinary shares. Basic earnings per share are calculated by dividing the profit or loss attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the period.

Diluted earnings per share are calculated by dividing the profit or loss attributable to ordinary and preference shareholders by the weighted average number of ordinary shares outstanding during the period decreased by potential shares arising from realised options.

j) Dividend distribution

Dividends are recognised in the statement of changes in equity and recorded as liabilities in the period in which they are approved by the Group's shareholders.

k) Foreign currency transactions

Foreign currency transactions are initially converted into Croatian kuna by applying the exchange rates prevailing on the transaction date. Cash, receivables and liabilities denominated in foreign currencies are re-translated at the rates prevailing on the balance sheet date. Gains and losses arising on translation are included in the income statement for the current year. Foreign exchange losses and gains arising on translation are included in profit or loss for the current year and are presented in Notes 13 and 14 in gross amounts (the stated amounts include foreign exchange differences from principal activities as well as foreign exchange differences on borrowings).

At consolidation, assets and liabilities of Group's foreign operations are translated into the Group presentation currency at the exchange rates prevailing at the balance sheet date. Income and expenses are translated at the average foreign exchange rate for the period and the foreign exchange differences are recognised in other comprehensive income. All foreign exchange differences are recognised as income or expense of the period in which the transaction occurred.

l) Non-current intangible and tangible assets (property, plant and equipment)

Non-current intangible and tangible assets are initially carried at cost, which includes the purchase price, including import duties and non-refundable tax after deducting trade discounts and rebates, as well as all other costs directly attributable to bringing the assets to their working condition for their intended use.

Non-current intangible and tangible assets are recognised if it is probable that future economic benefits associated with the item will flow to the Group and if the cost of the asset can be reliably measured.

After initial recognition, assets are measured at cost less accumulated amortisation and depreciation and any accumulated impairment losses.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Maintenance and repairs, replacements and minor-scale improvements are expensed when incurred. In situations where it can be clearly demonstrated that the expenditures have resulted in an increase in future economic benefits expected to be obtained from the use of an asset beyond its originally assessed standard performance, the expenditures are capitalised i.e. included in the carrying value of the asset. Gains or losses on the retirement or disposal of assets are included in the income statement in the period when incurred.

The amortisation and depreciation of assets commence when the assets are ready for use, i.e. when the assets are at the required location and the conditions necessary for use have been met. The amortisation and depreciation of assets cease when the assets are fully amortised or depreciated and expensed or classified as held for sale. Amortisation and depreciation are charged so as to write off the cost of each asset, other than land and non-current intangible and tangible assets under construction, over their estimated useful lives, using the straight line method.

	Amortisation and depreciation rates (from - to)
Concessions, patents, licences, software etc.	25%
Buildings	3% - 5%
Plant and equipment	5% -25%
Tools	5% - 25%

Impairment of property, plant and equipment

At each balance sheet date, the Group reviews the carrying amount of its property, plant and equipment to determine whether there is any indication that those assets should be impaired. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of the individual asset, the Group estimated the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest Group's cash-generating units for which a reasonable and consistent allocation basis can be identified.

The recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to an asset.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately as an expense in the income statement.

m) Leases

Leases are classified as finance leases whenever all the risks and rewards of ownership are substantially transferred to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are initially recognised as assets in the lessee's balance sheet at the fair value of the leased asset or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Lease payments are apportioned between finance costs and reduction of the lease obligations so as to achieve a constant rate of interest on the remaining balance of the liability. Finance costs are charged directly to profit or loss.

Operating lease payments are recognised in profit or loss as an expense on a straight-line basis over the lease term.

n) Inventories

Inventories are stated at the lower of cost or net realisable value. The cost of inventories comprises all purchase costs, cost of conversion and other costs that have been incurred in bringing the inventories to their present location and condition. Cost is calculated using the weighted average cost method.

Costs of conversion comprise costs that are specifically attributable to units of production such as direct labour and similar. They also comprise a systematic allocation of fixed and variable production overheads incurred in converting raw materials into finished goods. Fixed production overheads are indirect costs of production that remain relatively constant r regardless of the level of production, such as depreciation, maintenance of factory buildings, the costs of factory management and similar. Variable production overheads are those that vary directly with the volume of production such as indirect materials and indirect labour.

The allocation of fixed production overheads is based on the normal level of productive capacity. The normal level of capacity is the average production expected to be achieved over a number of periods in normal circumstances, taking into account a production loss due to planned maintenance. Unallocated overheads are expensed in the period in which they are incurred.

Slow moving and obsolete inventories are written off to its net realisable value by using value adjustment account for these inventories. Net realisable value is the estimated net selling price in the normal course of business decreased by estimated cost of completion and estimated costs needed to complete the sale.

Small inventories, packaging and car tyres are fully written off when put into use.

o) Receivables

Receivables are initially measured at fair value. At each balance sheet date, receivables, whose collection is expected within a period of more than one year, are stated at amortised cost using the effective interest method, less any impairment loss. Current receivables are stated at the initially recognised nominal amount less the corresponding impairment allowance for the expected credit losses and impairment losses.

p) Cash and cash equivalents

Cash consists of bank demand deposits, cash on hand and deposits and securities payable on demand or at the latest within a period of three months.

q) Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated

at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the statement of comprehensive income over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date.

r) Provisions

Provisions are recognised only when the Group has a present obligation as a result of a past event; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount can be reliably estimated. Provisions are reviewed at each balance sheet date and adjusted to reflect the best current estimate.

Provisions are determined for costs of repairs within warranty periods, awards to employees for long-term employment and retirement (regular jubilee awards and termination benefits).

Provisions for warranties are recognised at the moment the underlying products are sold. Provisions are made based on estimates and experiences of the Group and other manufacturers of energy transformers within the Group and the estimate of possible solutions in accordance with their probabilities.

Provisions for employee benefits for the number of years of service and retirement (regular jubilee awards and termination benefits) are determined as the present value of future cash outflows using a discount rate equal to the interest rate on government bonds.

s) Employee benefits

(i) Defined pension fund contributions

In the normal course of business through salary deductions, the Group makes payments to mandatory pension funds on behalf of its employees as required by law. All contributions made to the mandatory pension funds are recorded as salary expense when incurred. The Group does not have any other pension scheme and, consequently, has no other obligations in respect of employee pensions.

(ii) Long-term employee benefits

The Group has post-employment benefits to be paid to the employees at the end of their employment in the Group (either upon retirement, termination or voluntary departure). The Group recognises a liability for these long-term employee benefits evenly over the period the benefit is earned based on actual years of service. The long-term employee benefit liability is determined using assumptions regarding the likely number of staff to whom the benefit will be payable, estimated benefit cost and the discount rate.

(ii) Short-term employee benefits - bonuses

A liability for employee benefits is recognised in provisions based on the Group's formal plan and when past practice has created a valid expectation by the Management Board/key employees that the bonus will be paid and the amount can be determined before the time of issuing the financial statements. Liabilities for bonus plans are expected to be settled within 12 months of the balance sheet date and are recognised at the amounts expected to be paid when they are settled.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

t) Contingent assets and liabilities

Contingent liabilities are not recognised in the financial statements. They are only disclosed in the notes to the financial statements, unless the probability of an outflow is insignificant.

Contingent assets are not recognised in the Group's consolidated financial statements, unless the realisation of income is certain and these assets are not contingent assets and can be recognised.

u) Events after the balance sheet date

Events after the balance sheet date, which provide additional information on the Group's position at the balance sheet date (adjusting events), are reflected in the financial statements. Events that are not adjusting events are disclosed in the notes to the financial statements, if material.

v) Adoption of new accounting policies

The Group adopted IFRS 15 and IFRS 9 for the first time. The nature and effects of the changes resulting from the adoption of new standards are set out below.

A. Financial assets and liabilities

A financial instrument is any contract that gives rise to both a financial asset of one entity and a financial liability or equity instrument of another entity.

Classification and measurement of financial assets

Financial assets are classified into three categories depending on the selected business model of financial asset management and the contractual cash flow characteristics:

- financial assets carried at amortised cost,
- financial assets at fair value through other comprehensive income and
- financial assets at fair value through profit or loss.

A business model for financial asset management depends on how the Group manages financial assets for the purpose of generating cash flows. Reclassification of debt instruments is only possible if the business model changes.

Business models for managing financial assets include:

- amortised cost model - business model whose objective is to hold a financial asset in order to collect contracted cash flows (principal and interest),
- the fair value model through other comprehensive income - business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and
- fair value model through profit or loss - business model whose objective is to hold a financial asset for trading or for managing the financial asset on a fair value basis.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Derecognition of financial assets

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and financial liability for the proceeds received.

On derecognition of financial assets at fair value through profit or loss, all gains or losses arising from the derecognition of such assets are recognised in profit or loss.

On derecognition of financial assets carried at fair value through other comprehensive income (other than equity instruments classified in this category), cumulative gains or losses previously recognised in other comprehensive income are reclassified and transferred from equity to profit or loss.

On derecognition of equity instruments classified as financial assets at fair value through other comprehensive income, amounts previously recognised in other comprehensive income are not reclassified to profit or loss.

On derecognition of financial assets at amortized cost, all gains or losses on termination of recognition are recognised in the income statement.

Impairment of financial assets

At each reporting date, for financial assets (except at fair value through the profit or loss), the Group recognises impairment allowances using the expected loss credit model.

The expected credit losses are estimated on an individual or a portfolio basis in a way that reflects:

- an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes,
- time value of money and
- all reasonable and supportable information that is available (without undue cost and effort) about past events, current conditions and forecasts of future conditions and circumstances.

Provisions for the impairment of trade receivables and contract assets are measured in the amount of lifetime expected credit losses, i.e. by applying a simplified approach to expected credit losses.

In measuring the expected credit losses, the Group uses historical observations (over a minimum period of 3 years) on days past due with regard to the collection of receivables adjusted for estimated future expectations for the collection of receivables. Trade receivables are divided into portfolios depending on the rating of the customer's domicile country and age structure.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

In addition to the above assets to which a simplified approach is applied, at subsequent measurement of financial assets, when determining the credit loss assessment, a general impairment approach is applied consisting of three stages: Stage 1, Stage 2 and Stage 3.

- Stage 1 - when determining the impairment of financial assets, a 12-month expected credit loss model is applied. This model applies if there is no significant increase in credit risk.
- Stage 2 - when determining the impairment of financial assets, a lifetime ECL model applies. This model applies if there is a significant increase in credit risk.
- Stage 3 - when determining the impairment of financial assets, a lifetime ECL model is applied. This model applies if there is a significant increase in credit risk and there is objective evidence of impairment at the reporting date.

For the amount of expected credit losses, the value of the financial asset is impaired and the gain or loss on the impairment is recognised in profit or loss, except for debt instruments where the credit losses are recognised in profit or loss but the carrying amount is not impaired, instead revaluation reserves are recognised.

Objective evidence of impairment of financial assets for expected credit losses includes:

- significant financial difficulties of the issuer or debtor and/or
- breach of contract, such as a default or delinquency in interest or principal payments; or
- probability that the borrower will enter bankruptcy or financial restructuring and/or

The past due presumption itself is not an absolute indicator that credit risk has increased after initial recognition. The assumption that there has been a significant increase in credit risk after initial recognition due to default may be refuted by the company if it has reasonable and supportable information that there has been no significant increase in credit risk, but this may be an indicator of an increase in credit risk unless there is no other information available.

Financial liabilities and equity instruments

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

An equity instrument is any contract that evidences a residual interest in the Group's assets after deducting all of its liabilities. Equity instruments issued by the Group are recorded at the proceeds received, net of direct issue costs.

Share capital

Ordinary shares

Share capital represents the nominal value of shares issued.

The share premium includes the premium at the issuance of shares. Transactions costs directly attributable to the issue of ordinary shares are recognised as a deduction from equity.

Reserves are stated at nominal amounts defined in the allocation of earnings, especially legal reserves, statutory reserves and other reserves.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Share capital repurchase

The consideration paid for the repurchase of the Group's equity share capital, including any directly attributable incremental costs related to the repurchase, is deducted from equity. Repurchased shares are classified as treasury shares and presented as a deduction from total equity. The purchase of treasury shares is recorded at cost, and the sale of treasury shares at the negotiated prices. The gain or loss from the sale of treasury shares is recognised directly in equity.

Financial guarantee contract liabilities

Financial guarantee contract liabilities are measured initially at their fair values and are subsequently measured at the higher of:

- the amount of the obligation under the contract, as determined in accordance with IAS 37 and
- the amount initially recognised less, where appropriate, cumulative effect recognised in accordance with the revenue recognition policies.

Financial liabilities, classification and measurement

Financial liabilities, including borrowings that are initially measured at fair value, net of transaction cost. They are subsequently measured at amortised cost using the effective interest method, with an interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments over the expected life of the financial instrument, or, where appropriate, a shorter period, to the gross carrying amount of the financial assets or to the amortised cost of financial liability, except for the credit-impaired financial assets.

Financial liabilities are classified as financial liabilities at fair value through profit or loss where the financial liability is either held for trading or designated by the Group as such.

They are measured at fair value and the associated profit or loss is recognised through profit or loss, except for the changes in the fair value of the liabilities resulting from the changes in the Company's own credit risk which are recognised in other comprehensive income. The net gain or loss recognised in the income statement includes any interest paid on the financial liability.

Derecognition of financial liabilities

A financial liability is derecognised when, and only when, it is discharged, cancelled or expires.

Effects

The Group applied the new rules retrospectively from 1 January 2018, with the practical expedients permitted under the standard.

In accordance with the permitted practice under IFRS 9, the Group has not restated the comparative information and it are presented in accordance with IAS 39. The information presented for 2017 and 2018 is not comparable since it has been prepared in accordance with different accounting policies as described in the notes. Consequently, the revised requirements under IFRS 7 Financial Instruments, Disclosures apply only to the current period.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Differences arising from the adoption of IFRS 9 have been recognised directly in retained earnings. The Group has not recognised the differences resulting from IFRS 9 adoption as they are not material.

The nature of the reconciliation is explained below:

	Total under IAS 39	Amortised cost	Fair value through profit or loss	Fair value through other comprehensive income
	HRK'000	*HRK'000*	*HRK'000*	*HRK'000*
Classification under IAS 39				
Loans and receivables				
Trade receivables	113,416	113,416	-	-
Receivables from related customers	42,907	42,907	-	-
Cash and cash equivalents	130,043	130,043	-	-
Available-for-sale assets				
Non-current financial assets	2,804	-	-	2,804
Assets at fair value through P&L				
Derivative financial assets - non-current	58	-	58	-
Derivative financial assets - current	883	-	883	-
	290,111	**286,366**	**941**	**2,804**

a) Classification and measurement

- The Group's investments that were classified as available for sale as at 31 December 2017 meet the criteria to be classified at fair value in other comprehensive income (FVOCI) and are classified as assets at fair value through other comprehensive income as at 1 January 2018.
- Non-current financial assets, current financial assets, trade receivables, cash and cash equivalents classified as loans and receivables at 31 December 2017 meet the criterion that contractual cash flows on debt instruments represent solely payment of principal and interest and are classified accordingly as assets at amortised cost as at 1 January 2018.
- The Group continued to measure all financial assets at fair value previously classified at fair value in accordance with IAS 39.

There is no impact on the Group's accounting for financial liabilities, as the new requirements only affect the accounting for financial liabilities that are designated at fair value through profit or loss and the Group does not have any such liabilities.

b) Impairment

The Group did not recognise additional impairment losses on assets at amortised cost and equity instruments at fair value through other comprehensive income because the analysis carried out showed that they are not material for the financial statements. The impairment has not changed the value of equity instruments in the balance sheet since they are still measured at fair value.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

B. Revenue recognition

The Group recognises revenue from:

- Sales of distribution transformers
- Sales of medium power transformers
- Sales of services

The Group recognises revenue when control over particular goods or services is transferred on to a customer, i.e. when a customer acquires the right to manage the transferred goods or services provided that there is an agreement that creates the enforceable rights and obligations and, among other things, where collection of the consideration is probable, taking into account the credit quality of the Group's customers. The revenue is recognised in the amount of transaction price the Group expects in return for the transfer of the promised goods or services to customers.

The promised consideration includes fixed amounts.

Sales of services: Revenue is recognised over time on a straight-line basis or as services are provided, i.e. according to the measurement of expenses incurred up to a certain date in relation to the total expected costs required for performance of the contract obligations as described in the previous section.

Sales of goods: Revenue is recognised at a time when control of goods passes to the buyer, usually after the delivery of the goods. Invoices are issued at that time and are usually paid within the deadlines defined by the contractual provisions.

When a party to a contract with a customer meets its obligation, contracts with customers are presented as a contract liability, contract asset or receivable in the statement of financial position, depending on the relationship between the Group's performance and the customer's payment. Contract assets and liabilities are presented as short-term because they arose within the usual operating cycle.

Contract assets and liabilities

A contract liability is presented when a customer has paid the consideration before the Group transfers a good or service to the customer.

If the Group performs by transferring goods or services to a customer before the customer pays consideration and the Group's right to consideration is only subject to the passage of time before payment of the consideration is due, the receivable is recognised.

Contract assets are recognised if the right to consideration is subject to a condition (for example, performance of some other obligation).

The Group has adopted this standard partially retrospectively with the effective date on 1 January 2018, keeping the amounts relating to the previous periods and presented them in accordance with the previous standards, showing the cumulative effect of applying IFRS 15 as an adjustment of the initial equity with the date of the first application of the standard. In accordance with this method, the Group has selected to apply the standard to all contracts that were not completed as at the date of first application.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

	Note	IAS 31 December 2017 (carrying amount)	Reclassification	Re-measurement	IFRS 15 as at 1 January 2018
		HRK'000	*HRK'000*	*HRK'000*	*HRK'000*
Inventories	a)	200,446	-	11,753	212,199
Contract assets	b)	-	-	3,258	3,258
Total assets		**200,446**	**-**	**15,011**	**215,457**
Contract liabilities	a)	-	45,944	20,140	66,084
Advances received	c)	45,944	(45,944)	-	-
Total liabilities		**45,944**	**-**	**20,140**	**66,084**
Total effect on equity					
Retained earnings	a), b)	**-**	**-**	**(5,129)**	**(5,129)**

The nature of reconciliation as at 1 January 2018 and the reasons for significant changes in the statement of financial position as at 31 December 2018 and in the statement of comprehensive income for the year ended 31 December 2018 are presented as follows:

a) Inventories

When applying the 5-step model set out in IFRS 15, the Group determined that there were certain contracts that do not meet the criteria for recognition of income over time, that is, under the said contracts the revenue is recognised at a point in time. Accordingly, for the said contracts which were recognised by the Group based on stage of completion in the previous period, the Group increased the work in progress by HRK 14,375 thousand, increased the amount of the contract liability by HRK 20,139 and reduced the amount of retained earnings by HRK 5,764 thousand.

b) Contract assets

After applying the 5-step model, the Group determined that there were certain contracts that meet the terms of recognition over time and consequently increased the contract assets in the amount of HRK 3,258 thousand, reduced inventories in the amount of HRK 2,622 thousand and increased retained earnings in the amount of HRK 636 thousand.

c) Long-term advances received from the customer

The Group sells transformers, whose design and construction lasts in some cases for more than a year once the contract has been signed. Prior to the adoption of IFRS 15, the Group presented these advances as liabilities on received advances in the statement of financial position, and the interest expense has not been accrued. In accordance with IFRS 15, the Group has concluded that there is a significant component of financing for these contracts in which the customer chose to pay a portion of the transaction price when the contract was signed. The amount received for such contracts is considered a discounted transaction price that takes into account a significant component of the financing. It has been defined at the Group level that an amount exceeding more than 5% of the contract price is a significant financing component, depending on the contract type. Upon adoption of IFRS 15, a reclassification of liabilities from advances received to contract liabilities was recorded in the observed period.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

An overview of individual items of financial statements that were affected by the adoption of IFRS 9 and IFRS 15 as at and for the year ended 31 December 2018 is provided below. The adoption of IFRS 9 and IFRS 15 did not have a significant impact on the Group's other comprehensive income or on the Group's operating, investing or financial cash flows. The first column shows the amounts recorded in accordance with IFRS 9 and IFRS 15, and the second column shows the amounts that would have been recorded had IFRS 9 and IFRS 15 not been adopted:

Consolidated statement of comprehensive income for the period ended 31 December 2018

	31 December 2018 IFRS 9, IFRS 15	31 December 2018 IAS 39, IAS 18	Difference
	HRK	*HRK*	*HRK*
Revenue	941,582,401	934,829,934	6,752,467
Other operating income	1,053,437	1,053,437	-
Operating income	**942,635,838**	**935,883,371**	**6,752,467**
Increase in inventories of work in progress and finished goods	27,196,270	31,961,616	(4,765,346)
Cost of materials and energy	(624,292,688)	(624,292,688)	-
Cost of goods sold	(30,709,501)	(30,709,501)	-
Service costs	(76,956,000)	(76,956,000)	-
Staff costs	(137,857,964)	(137,857,964)	-
Depreciation and amortisation	(19,277,140)	(19,277,140)	-
Other expenses	(25,333,415)	(25,333,415)	-
Impairment	(2,105,516)	(2,105,516)	-
Losses on impairment of financial assets	(115,966)	(94,975)	(20,991)
Provisions	(3,612,210)	(3,612,210)	-
Other operating expenses	(1,461,435)	(1,461,435)	-
Operating expenses	**(894,525,565)**	**(889,739,228)**	**(4,786,337)**
Operating profit	**48,110,273**	**46,144,143**	**1,966,130**
Net finance result	**1,418,839**	**1,418,839**	**-**
Investments accounted for using the equity method	**593,218**	**593,218**	**-**
Profit before tax	**50,122,330**	**48,156,200**	**1,966,130**
Income tax	(1,499,222)	(1,499,222)	-
PROFIT FOR THE YEAR	**48,623,108**	**46,656,978**	**1,966,130**
Other comprehensive income	**(668,540)**	**(668,540)**	**-**
COMPREHENSIVE INCOME FOR THE YEAR	**47,954,568**	**45,988,438**	**1,966,130**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Consolidated statement of financial position as at 31 December 2018

	31 December 2018 IFRS 9, IFRS 15	31 December 2018 IAS 39, IAS 18	Difference
	HRK	*HRK*	*HRK*
ASSETS			
Non-current assets			
Intangible assets	2,651,830	2,651,830	-
Property, plant and equipment	168,536,805	168,536,805	-
Investment property	3,339,582	3,339,582	-
Investments accounted for using the equity method	4,821,718	4,821,718	-
Financial assets	2,838,665	2,838,665	-
Receivables	659,606	659,606	-
Deferred tax assets	231,150	231,150	-
	183,079,356	**183,079,356**	**-**
Current assets			
Inventories	264,066,649	257,078,663	6,987,986
Receivables from related parties	17,931,894	17,932,186	(292)
Trade receivables	183,102,787	183,123,486	(20,699)
Contract assets	8,160,665	-	8,160,665
Other receivables	4,765,582	4,765,582	-
Financial assets	293,340	293,340	-
Cash and cash equivalents	103,777,825	103,777,825	-
Prepaid expenses	558,914	558,914	-
	582,657,656	**567,529,996**	**15,127,660**
TOTAL ASSETS	**765,737,012**	**750,609,352**	**15,127,660**
EQUITY AND LIABILITIES			
Share capital	**153,369,600**	**153,369,600**	**-**
Legal reserves	3,839,641	3,839,641	-
Statutory reserves	76,684,800	76,684,800	-
Other reserves	45,982,991	45,982,991	-
Translation reserves	(423,053)	(423,053)	-
Retained earnings	**87,517**	5,216,160	(5,128,643)
Profit for the year	**48,623,108**	**46,656,978**	1,966,130
EQUITY	**328,164,604**	**331,327,117**	**(3,162,513)**
Provisions	**112,277,057**	**112,277,057**	**-**
Non-current liabilities	**34,359,282**	**34,359,282**	**-**
Liabilities to related parties	8,233,655	8,233,655	-
Bank borrowings	19,427,829	19,427,829	-
Trade payables	102,822,474	102,822,474	-
Contract liabilities	84,970,726	-	84,970,726
Advances received	-	63,066,933	(63,066,933)
Other liabilities	18,033,513	18,033,513	-
Accrued expenses and deferred income	2,077,684	5,691,304	(3,613,620)
Current provisions	55,370,188	55,370,188	-
Current liabilities	**290,936,069**	**272,645,896**	**18,290,173**
Total liabilities	**437,572,408**	**419,282,235**	**18,290,173**
TOTAL EQUITY AND LIABILITIES	**765,737,012**	**750,609,352**	**15,127,660**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

3. Critical accounting estimates

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

a) Revenue recognition

The Group recognises revenue at a point in time for delivery of goods since the asset created has an alternative use because it can be sold in the area of the same or similar energy network. This criterion will be even more pronounced in the future, due to the intention to harmonise energy networks in the EU.

Revenue is recognised when a customer obtains control of specific goods, usually when the goods are delivered, when the buyer has full discretionary powers over the goods and when there are no unsatisfied performance obligations that might affect the buyer's acceptance of the goods.

Delivery usually occurs when the goods are delivered to the agreed location and the risk of loss is transferred to the buyer and the buyer accepted the goods in accordance with the contractual provisions, or the terms of acceptance of the goods expired or if the company has objective evidence that all acceptance criteria have been met.

b) Extended warranties

The Group provides warranties for its products/projects performed for a period of 3 - 5 years. Management estimates the provision for costs of repair and correction of defects within warranty periods based on past experience. The Group analysed contracts in which a guarantee was issued beyond the above stated period and found that there were no significant non-standard guarantees and accordingly did not defer a portion of the transaction price over a time period other than the standard guarantee.

c) Significant financing component

In certain contracts, the Group contracted to sell the equipment whose production may last longer than one year after the signing of the contract. Depending on the type of product, the production can take up to 2 years. Accordingly, the period between payment by the buyer and the transfer of the promised goods or services to the buyer may be longer than one year. The amount received in advance for such contracts is considered a discounted transaction price. At the Group level it has been defined that a significant financing component is the amount exceeding 5% of the contract price, depending on the type of contract as well as the effective market interest rate. The Group does not adjust the promised amount of compensation in accordance with the effects of a significant financing component if the company concludes that the period between the transfer of the promised goods or services to the buyer and the date when the buyer is paying for the goods or services will last one year or less.

d Impairment of inventories

The Group performs an impairment of inventories for all inventories whose carrying amount exceeds the market value, i.e. realisable value. The estimate is based on the observable prices which can be achieved on the market involving this kind of industry (for example, prices of cuprum declined in 2018, and the Group recognised a provision for impairment for cuprum items on stock).

e) Warranty provisions

The Group provides warranties for its products for a period of 3-5 years. The Management Board estimates a provision for future warranty fees based on historical information. Factors that could impact the estimated claim information include the success of the Group's quality initiatives, as well as spare parts and labour costs. If the required level of general provisions made had increased by 1% in relation to performed deliverables in the past three years, provisions would have increased by HRK 25 million (2017: HRK 24 million).

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

4. Revenue

Revenue analysis by categories in accordance with the application of new revenue recognition guidance as at 1 January 2018:

	2018
	HRK
Type of goods or services	
Sales of distribution transformers	429,503,516
Sales of medium power transformers	490,067,418
Sales of services	22,011,467
Total revenue from Contracts with Customers	**941,582,401**
Geographic areas	
Croatia	154,879,236
European Union countries	625,705,219
Bosnia and Herzegovina; Macedonia, Serbia and Montenegro	21,203,813
Other European countries	75,504,091
Africa	34,479,867
Asia	24,210,382
Other countries	5,599,793
Total revenue from Contracts with Customers	**941,582,401**
Revenue recognition	
At a point in time	941,582,401
Total revenue from Contracts with Customers	**941,582,401**

Revenue analysis by categories in accordance with the revenue recognition guidance applicable until January 1, 2018:

	2017
	HRK
Foreign sales	760,517,828
Domestic sales	146,363,119
	906,880,947

Revenue by segments in 2017

	Medium power transformers	Distribution transformers	Total
	HRK	*HRK*	*HRK*
Sales to unrelated parties	480,729,694	332,680,682	813,410,376
Sales to related parties	51,350,340	42,120,231	93,470,571
	532,080,034	**374,800,913**	**906,880,947**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

5. Other operating income

	2018	2017
	HRK	*HRK*
Net gain on sale of non-current assets	427,557	511,098
Income from collected receivables previously written off	160,542	259,490
Inventory surpluses	199,354	227,187
Insurance reimbursements	93,390	15,797
Income from collected penalties, awards etc.	70,596	59,452
Income from approved discounts, rebates, etc.	28,077	45,798
Other income	73,921	1,117,183
	1,053,437	**2,236,005**

6. Cost of materials and energy

	2018	2017
	HRK	*HRK*
Raw materials and supplies consumed	616,776,705	537,798,757
Energy cost	6,391,375	5,742,852
Cost of small inventory	1,124,608	743,364
	624,292,688	**544,284,973**

7. Service costs

	2018	2017
	HRK	*HRK*
Transport services	20,497,852	21,231,089
External products design and selling services	15,336,056	15,510,605
Agent commission costs	10,460,057	9,666,394
Maintenance services (servicing)	9,595,801	9,644,868
Compensation for the usage of company name and trade mark - Končar Inc.	5,354,404	5,284,643
Entertainment	3,799,112	2,813,551
Intellectual and similar services	1,542,758	2,317,046
Outsourcing of employees	1,079,938	1,902,430
Telephone, post, etc.	1,583,763	1,555,795
Costs of advertising and fairs	1,034,342	1,133,812
Rent services and leases	1,069,082	1,024,425
Utility services	976,632	892,329
Audit costs	85,876	62,568
Other external costs	4,540,327	4,147,109
	76,956,000	**77,186,664**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

8. Staff costs

	2018	2017
	HRK	*HRK*
Net salaries and wages	78,908,692	71,799,735
Taxes and contributions	39,104,188	37,311,549
Contributions on salaries	19,845,084	18,819,212
	137,857,964	**127,930,496**

Net salaries in the amount of HRK 78,908,692 (2017: HRK 71,799,735) include compensations to members of the Management Board of the Company and the related companies, comprising the Management Board's salaries amounting to HRK 2.170.268 (2017: HRK 2,024,564) and the accrued Management bonus in the amount of HRK 1,971,450 (2017: HRK 1,910,790), and are an integral part of staff costs.

In 2018, pension fund contributions amounted to HRK 21,814,257 (2017: HRK 20,220,250).

Employee benefits (such as travel to and from work, termination benefits and jubilee awards, business travel expenses) in the amount of HRK 12,527,267 (2017: HRK 11,924,267) are disclosed in Note 10.

9. Depreciation and amortisation

	2018	2017
	HRK	*HRK*
Depreciation (Note 19)	18,125,481	18,589,247
Amortisation (Note 18)	991,242	1,028,222
Depreciation of investment property (Note 20)	160,417	-
	19,277,140	**19,617,469**

10. Other expenses

	2018	2017
	HRK	*HRK*
Bank charges and commissions	3,298,253	3,019,319
Employee transportation costs (Note 8)	3,955,099	3,821,184
Daily allowances for business trips and travel expenses (Note 8)	3,684,220	3,402,259
Compensations to employees, gifts and grants (Note 8)	2,969,902	2,709,614
Insurance premiums	2,336,228	2,122,060
Voluntary pension fund premiums and fees (Note 8)	1,918,313	1,991,210
Compensation to Supervisory Board members	422,473	471,193
Contributions, membership fees and similar charges	289,541	277,978
Other	6,459,386	5,917,676
	25,333,415	**23,732,493**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

11. Value adjustments (impairment losses)

	2018	2017
	HRK	*HRK*
Impairment of inventories	2,105,516	5,849,804
Impairment of non-current assets held for sale	-	500,000
	2,105,516	**6,349,804**

12. Provisions

	2018	2017
	HRK	*HRK*
Provisions for risks within warranty period	3,158,244	6,665,398
Provisions for termination benefits and jubilee awards	400,156	12,959,405
Provisions for penalties	-	1,243,762
Other provisions	53,810	156,880
	3,612,210	**21,025,445**

The movement in provisions by categories is presented in Notes 31 and 39.

13. Finance income

	2018	2017
	HRK	*HRK*
Related parties		
Foreign exchange gains	3,689	97,745
	3,689	**97,745**
Unrelated parties		
Foreign exchange gains	10,801,113	10,111,705
Dividend income and share in profit of associates	1,283,404	1,913,086
Interest income on term deposits	10,085	-
Other interest income	95,951	323,116
	12,190,553	**12,347,907**
	12,194,242	**12,445,652**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

14. Finance costs

	2018	2017
	HRK	*HRK*
Related parties		
Foreign exchange losses	163,126	159,526
	163,126	**159,526**
Urelated parties		
Interest expense on borrowing and other forms of financing	979,251	1,016,480
Foreign exchange losses	8,413,554	8,294,649
Foreign exchange losses on forward contracts	759,226	723,289
Other	460,246	-
	10,612,277	**10,034,418**
	10,775,403	**10,193,944**

15. Share in profit of associate

The share in profit of an associate in the amount of HRK 593,218 (2017: HRK 284,500) relates to the share in profit of the company Elkakon Ltd. in which the Group holds a 50% share.

In 2018, the said company realised a total net income of HRK 1,186,436 thousand. HRK 568,558).

16. Income tax

The Parent company calculates income tax at a preferential rate obtained when reducing the income tax rate by 85%, as the Parent company is the beneficiary of incentive measures in accordance with the Investment Promotion Act for a project entitled "High-Voltage Laboratory - Laboratory development and extension of production capacities". On 3 September 2010, the Ministry of Economy, Labour and Entrepreneurship issued a certificate confirming that these investments meet the requirements of the Act and that the Parent company may use the incentive measures. The maximum amount of the granted incentive is HRK 37,327,421.

On 6 October 2014, the Ministry of Economy issued an Approval for the revision of the maximum amount of the granted incentive for the "High-Voltage Laboratory" project due to increased invested financial funds and an increased number of newly created jobs in relation to the planned ones. The new maximum amount of the granted investment incentive amounts to HRK 63.437.498, and the cumulative amount used to date is HRK 49.843.342. The Group has not yet used maximum of the granted incentive whitch has to be used until 2020. The Group does not expect to use the total maximum of the granted incentive received for this investment by this point in time.

	2018	2017
	HRK	*HRK*
Current tax	1,501,377	1,779,573
Deferred tax (difference)	(2,155)	(228,995)
Income tax expense	**1,499,222**	**1,550,578**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

The Group's current income tax differs from the theoretical amount that would arise using the actual tax rate applicable to profits of the Group as follows:

	2018	2017
	HRK	*HRK*
Consolidated profit before tax	50,122,330	45,913,982
Income tax at 18% (2017: 18%)	9,022,019	8,264,517
Adjustments for tax effects from:		
Consolidation adjustments	100,526	(514,060)
Non-deductible expenses	2,286,674	4,651,814
Tax deductions	(1,400,040)	(538,450)
Investment incentives (2018: 85%; 2017 85%)	(8,507,802)	(10,084,248)
Current income tax charge	**1,501,377**	**1,779,573**
Effective tax rate	3.00%	3.87%
Advances paid	1,480,140	766,264
Income tax payable	21,237	1,013,309

17. Earnings per share

Basic earnings per share:

	2018	2017
	HRK	*HRK*
Net profit	48,623,108	44,363,404
Number of shares		
Total number of shares for the entire year	255,616	255,616
Capitalisation at 17 September 2018 (Note 30)	255,616	255,616
Number of shares	**511,232**	**511,232**
Earnings per share	**95.11**	**86.78**

In the previous years the distributed dividends for ordinary and preference shares were the same. The Group does not have any treasury shares.

Diluted earnings per share

Diluted earnings per share for 2018 and 2017 are the same as basic since the Group had no convertible instruments or options during both periods.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

18. Non-current intangible assets

	Concessions, patents, licences, software and other rights	Assets under construction	Total
	HRK	*HRK*	*HRK*
Cost			
At 1 January 2017	**10,436,240**	**-**	**10,436,240**
Acquisition of subsidiary	42,057	-	**42,057**
Additions	-	447,000	**447,000**
Transfer	447,000	(447,000)	**-**
Disposals	(2,780)	-	**(2,780)**
At 31 December 2017	**10,922,517**	**-**	**10,922,517**
Additions	33,679	1,212,834	**1,246,513**
Transfer	1,212,834	(1,212,834)	**-**
Disposals		-	**-**
At 31 December 2018	**12,169,030**	**-**	**12,169,030**
Accumulated amortisation			
At 1 January 2017	**7,500,516**	**-**	**7,500,516**
Amortisation charge for the year	1,028,222	-	**1,028,222**
Disposals	(2,780)	-	**(2,780)**
At 31 December 2017	**8,525,958**	**-**	**8,525,958**
Amortisation charge for the year	991,242	-	**991,242**
At 31 December 2018	**9,517,200**	**-**	**9,517,200**
Net book amount			
31 December 2017	2,396,559	-	**2,396,559**
31 December 2018	**2,651,830**	**-**	**2,651,830**

The cost of intangible assets fully amortised and still in use as at 31 December 2018 amounts to HRK 5,116,680 (2014: HRK 5,113,167).

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

19. Property, plant and equipment

	Land	Buildings	Plant and equipment	Tools and office supplies	Advances	Assets under con-struction	Total
Cost	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*
At 1 January 2017	**9,012,529**	**124,867,770**	**190,523,613**	**28,016,197**	**595,554**	**4,389,827**	**357,405,490**
Acquisition of subsidiary	2,105,083	15,745,105	3,552,215	702,863	-	1,439,801	**23,545,067**
Additions	-	2,609,683	-	-	3,589,005	9,253,802	**15,452,490**
Transfer to use	-	2,962,288	7,796,162	2,805,855	-	(13,564,305)	**-**
Disposals	-	-	(1,756,803)	(2,367,373)	(3,428,951)	-	**(7,553,127)**
At 31 December 2017	**11,117,612**	**146,184,846**	**200,115,187**	**29,157,542**	**755,608**	**1,519,125**	**388,849,920**
Additions	-	47,794	-	-	10,453,732	18,580,561	**29,082,087**
Transfer to use	-	669,215	9,561,762	1,961,914	-	(12,192,891)	**-**
Disposals	-	-	(1,043,326)	(1,886,238)	(4,290,387)	-	**(7,219,951)**
Foreign exchange differences	(86,303)	(1,069,174)	300,596	(18,794)	-	(65,765)	**(939,440)**
At 31 December 2018	**11,031,309**	**145,832,681**	**208,934,219**	**29,214,424**	**6,918,953**	**7,841,030**	**409,772,616**
Accumulated depreciation							
At 1 January 2017	**-**	**68,961,449**	**123,787,470**	**18,845,741**	**-**	**-**	**211,594,660**
Acquisition of subsidiary	-	(399,823)	-	-	-	-	**(399,823)**
Depreciation charge for the year	18,532	5,737,128	10,078,971	2,754,616	-	-	**18,589,247**
Disposals	-	-	(1,687,844)	(2,367,373)	-	-	**(4,055,217)**
At 31 December 2017	**18,532**	**74,298,754**	**132,178,597**	**19,232,984**	**-**	**-**	**225,728,867**
Depreciation charge for the year	17,765	5,796,709	9,833,268	2,477,739	-		**18,125,481**
Disposals	-	-	(904,074)	(1,714,463)	-		**(2,618,537)**
At 31 December 2018	**36,297**	**80,095,463**	**141,107,791**	**19,996,260**	**-**		**241,235,811**
Net book amount							
31 December 2017	11,099,080	71,886,092	67,936,590	9,924,558	755,608	1,519,125	163,121,053
31 December 2018	**10,995,012**	**65,737,218**	**67,826,428**	**9,218,164**	**6,918,953**	**7,841,030**	**168,536,805**

As at 31 December 2017, the net book amount of mortgaged properties amounts to HRK 76,182,480 (31 December 2017: HRK 66,538,481). Mortgages have been registered over these properties in the total amount of EUR 40 million, and there is a pledge on movable assets (net carrying amount of HRK 14.9 million) in the amount of EUR 25 million (31 December 2017: EUR 25 million) (Note 30).

The cost of fully depreciated tangible assets still in use as at 31 December 2017 amounts to HRK 82,990,105 (31 December 2017: HRK 90,042,028).

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

20. Investment property

Cost	*HRK*
At 1 January 2017	**-**
Transfer from non-current assets held for sale	4,000,000
At 31 December 2017	**4,000,000**
Additions	-
At 31 December 2018	**4,000,000**
Accumulated depreciation	
At 1 January 2017	**-**
Impairment	500,000
Depreciation charge for the year	-
At 31 December 2017	**500,000**
Depreciation charge for the year	160,418
At 31 December 2018	**660,418**
Net book amount	
31 December 2017	3,500,000
31 December 2018	**3,339,582**

21. Investments accounted for using the equity method

	31 December 2018	**31 December 2017**
	HRK	*HRK*
Investment in associate		
Elkakon Ltd., Zagreb (50% share)	4,821,718	4,368,500
Total	**4,821,718**	**4,368,500**

The company Elkakon produces industrial conductors and is primarily the strategic partner to the subsidiary Končar D&ST d.d.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

	Elkakon Ltd.	
	2018	**2017**
	HRK'000	*HRK'000*
Revenues	76,854	67,181
Expenses	75,407	66,476
Profit before tax	1,447	705
Income tax	(261)	(136)
Profit after tax	**1,186**	**569**
Non-current assets	9,245	5,691
Current assets	19,390	16,025
Total assets	**28,635**	**21,726**
Total liabilities	**18,992**	**12,979**

Movements in investments in associates during the year were as follows:

	Elkakon Ltd.
	HRK
1 January 2017	**4,284,000**
Profit of associate (Note 15)	284,500
Dividend payment by associate	(200,000)
31 December 2017	**4,368,500**
Profit of associate (Note 15)	593,218
Dividend payment by associate	(140,000)
31 December 2018	**4,821,718**

22. Non-current financial assets

	31 December 2018	31 December 2017
	HRK	*HRK*
Financial assets at fair value through other comprehensive income		
Shares in companies up to 20% of the share capital		
Ferokotao Ltd., Donji Kraljevec (16% share)	1,048,128	1,048,128
Novi Feromont Ltd., Donji Kraljevec (18.9% share)	1,717,200	1,717,200
	2,765,328	**2,765,328**
Financial assets at fair value through profit or loss		
Shares in Zagrebačka banka d.d., Zagreb	**39,000**	**39,000**
Derivative instruments - FX Forward contracts	**34,337**	**57,782**
	2,838,665	**2,862,110**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

23. Inventories

	31 December 2018	31 December 2017
	HRK	*HRK*
Raw materials and supplies	101,179,152	74,351,756
Work in progress	96,317,130	72,479,376
Unfinished and semi-finished goods	4,676,874	7,342,814
Finished goods	71,586,549	54,160,924
Less: Impairment of raw materials and supplies	(5,624,026)	(4,082,390)
Less: Impairment of finished goods	(6,236,041)	(5,680,741)
	261,899,638	**198,571,739**
Advances given	2,167,011	1,873,815
	264,066,649	**200,445,554**

In 2018, the cost of own goods sold amounted to HRK 651,990,508 (2017: HRK 644,581,545).

24. Receivables from related parties

	31 December 2018	31 December 2017
	HRK	*HRK*
Sister companies within the Končar Group:		
Končar - Power Plant and Electric Traction Engineering Inc. Zagreb	9,148,976	28,469,694
Končar - Končar - Switchgear Inc., Zagreb	823,700	687,802
Končar - Electronics and Informatics Inc., Zagreb	219,000	-
Končar - Electrical Engineering Institute Inc., Zagreb	28,250	-
Končar - Electrical Vehicles Inc., Zagreb	13,029	-
Končar - Instrument Transformers Inc., Zagreb	750	750
Impairment of receivables from related parties	**(286)**	**-**
	10,233,419	**29,158,246**
Associates:		
Elkakon d.o.o., Zagreb	7,432,299	6,791,986
Končar - Power Transformers, Ltd., Zagreb	266,176	6,956,616
Impairment of receivables from related parties	-	-
	7,698,475	**13,748,602**
	17,931,894	**42,906,848**

As at 31 December, the ageing structure of receivables from the Group's related parties was as follows:

	Total	Not past due	Past due but collectible				
			< 60 days	60-90 days	90-180 days	180-365 days	> 365 days
	HRK	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*
2018	**17,931,894**	12,519,661	2,492,328	-	-	2,919,905	-
2017	**42,906,848**	41,921,544	629,300	-	257,852	98,152	-

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

25. Trade receivables

	31 December 2018	31 December 2017
	HRK	*HRK*
Domestic trade receivables	33,697,182	29,905,883
Less: Provision for impairment	(3,489,812)	(3,648,697)
	30,207,370	**26,257,186**
Foreign trade receivables	153,932,710	88,547,476
Less: Provision for impairment	(1,037,293)	(1,388,724)
	152,895,417	**87,158,752**
	183,102,787	**113,415,938**

As at 31 December, the ageing structure of the Group's trade receivables was as follows:

	Total	Not past due	Past due but collectible				
			< 60 days	60-90 days	90-180 days	180-365 days	> 365 days
	HRK	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*
2018	**183,102,787**	145,387,136	27,119,704	8,546,887	748,839	532,040	768,181
2017	**113,415,938**	86,761,025	18,584,669	647,451	1,648,534	5,720,088	54,171

The maximum exposure to credit risk at the balance sheet date is the carrying value of each class of receivables mentioned above.

The following table explains the changes in the credit loss allowance for trade receivables under simplified ECL model between the beginning and the end of the period:

	2018
	HRK
Opening balance at 1 January 2018	5,037,421
Increase in the expected credit loss during the year	115,966
Collected receivables	(170,178)
Total movement in the expected credit losses through profit or loss	**(54,212)**
Written-off during the year	(428,140)
Foreign exchange differences	(27,964)
At 31 December	**4,527,105**

The effect of the first adoption of the IFRS 9 simplified approach on trade receivables is not material and as such was not recorded as at 1 January 2018.

The movement in the impairment of the Group's trade receivables was as follows:

	2017
	HRK
At 1 January	5,347,294
Acquisition	9,701
Collected during the year	(259,490)
Written off during the year	(51,983)
Written off during the year (foreign exchange difference)	(8,101)
At 31 December	**5,037,421**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

26. Contract assets and liabilities

	31 December 2018	1 January 2018
	HRK	*HRK*
Contract assets from Contracts with Customers	-	3,257,505
Total current assets from Contracts with Customers	**-**	**3,257,505**
Current assets recognised for costs incurred to obtain a contract	**8,160,665**	**-**
Contract liability from Contracts with Customers	10,129,508	20,139,480
Contract liability - advances received from customers	63,066,394	45,943,641
Accrued agent commissions	3,614,159	-
Contract liability arising from agent commissions	8,160,665	-
Total contract liabilities	**84,970,726**	**66,083,121**

Revenue recognised in relation to contract liabilities

Revenue recognised in the reporting period, which was included in the contract liability balance at the beginning of the period, related to the design and construction services of the plant and equipment for production, transmission and distribution of electricity, amounted to HRK 20,139 thousand.

The total amount of transaction price allocated to the performance obligations not satisified (or partially satisfied) at the end of the reporting period amount to HRK 10,129 thousand.

The Company's management expects that 100% of the transaction price allocated to the unsatisfied contracts as of 31 December 2018 will be recognised as revenue during the next reporting period (HRK 10,129 thousand).

All other contracts in which the Group is entitled to a consideration from the customer in an amount that directly corresponds to the benefits received by the buyer from the Company's performance for the periods of one year or less is recognised by the Company in the amount it is entitled to bill. As permitted under IFRS 15, the transaction price allocated to these unsatisfied contracts is not disclosed.

27. Other receivables

	31 December 2018	31 December 2017
	HRK	*HRK*
VAT receivable	3,850,584	1,451,780
Other receivables	914,998	1,281,071
	4,765,582	**2,732,851**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

28. Current financial assets

	31 December 2018	31 December 2017
	HRK	*HRK*
Other current financial assets		
Derivative instruments - FX forward contracts	293,340	882,706
	293,340	**882,706**

29. Cash and cash equivalents

	31 December 2018	31 December 2017
	HRK	*HRK*
Foreign currency accounts balance	59,600,467	119,999,504
HRK currency accounts balance	44,104,382	9,991,902
Cash in hand - foreign currencies	42,026	35,857
Cash in hand - HRK	30,950	16,136
	103,777,825	**130,043,399**

Disclosures relating to credit risk are presented in the note Financial instruments.

30. Capital and reserves

Share capital is determined in the nominal amount of HRK 153,369,600 (31 December 2017: HRK 76,684,800) and comprises 511,232 shares with a nominal value of HRK 300 per share. 255,616 shares).

The General Assembly of Končar D&ST held on 28 May 2018 made a decision to increase the share capital from reserves. By the decision of the General Assembly, the share capital was increased by converting the statutory reserves from HRK 76,684,800 to HRK 153,369,600 by issuing new 255,616 shares and the total number of shares after the new issue was 511,232 shares (out of which 388,376 ordinary KODT-RA shares and 122,856 preferential KODT-PA shares, each with the nominal value of HRK 300). Shareholders of the Parent company obtained new shares in proportion to their participation in the Parent company's existing share capital.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

The ownership structure of the Parent company is as follows:

	31 December 2018		31 December 2017	
Dioničar	*Number of shares*	*Share in ownership %*	*Number of shares*	*Share in ownership %*
Končar- Electrical Industry Inc.	269,596	52.73	134,798	52.73
AZ OMF B category	27,100	5.3	13,550	5.3
Knežević Nikola	21,304	4.17	7,852	3.07
Floričić Kristijan	19,832	3.88	9,916	3.88
Radić Antun	7,886	1.54	3,943	1.54
AZ Mandatory Pension Fund A category	7,604	1.49	3,628	1.42
Other	157,910	30.89	79,129	30.96
SZAIF d.d.	-	-	2,800	1.1
	511,232	**100.00**	**255,616**	**100.00**

As at 31 December 2018, the Parent company's share capital consists of 388,376 ordinary shares and 122,856 preference shares (31 December 2017: 194,188 ordinary shares and 61,428 preference shares).
The dividend per share paid to the Parent company's shareholders in 2018 amounted to HRK 81.20 per share (2017: HRK 56.23 per share).
Statutory, legal and other reserves were formed on the basis of profit distribution compliant with the decisions of the General Assembly, in accordance with the provisions of the Companies Act (statutory and other reserves are eligible for distribution pursuant to the provisions of the above Act and the Company's Articles of Association).

31. Provisions

	Warranty provisions	Jubilee awards and termination benefits	Total
	HRK	*HRK*	*HRK*
1 January 2017	**95,836,420**	**2,255,022**	**98,091,442**
Additional provisions	6,665,398	12,959,405	19,624,803
Acquisition	817,669	-	817,669
Foreign exchange differences	-	10,007	10,007
Transfer to current provisions	(3,694,695)	-	(3,694,695)
31 December 2017	**99,624,792**	**15,224,434**	**114,849,226**
Additional provisions	2,194,941	400,156	2,595,097
Foreign exchange differences	15,214	(15,593)	(379)
Transfer to current provisions	(5,166,887)	–	(5,166,887)
31 December 2018	**96,668,060**	**15,608,997**	**112,277,057**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Warranty provisions

Warranty provisions are determined on the basis of Management's best estimate and includes general and specific provisions. General provisions are based on estimates and experience of other similar producers of transformers. The Group regularly issues warranties for a minimum of 3 years for each sold transformer. Management assesses and recognises a provision representing 2% of the value of sold products under warranty obligation (2017: 2%). Specific provisions refer to potential quality issues with regard to sold transformers to individual customers in the total amount of HRK 95 million (2017: HRK 96 million).

Provisions for long-term employee benefits (termination benefits and jubilee awards)

The non-current portion of termination benefits and jubilee awards in the amount of HRK 15,608,997 (2017: HRK 15,224,434) relates to the estimated amount of termination benefits and jubilee awards in line with the Collective Agreement, to which Company employees are entitled at the end of their employment (either upon retirement, termination or voluntary departure, meeting the conditions for obtaining jubilee awards). The present value calculation of these provisions is based on the number of employees, average gross salary, number of years of service at the Company and the statistics of paid termination benefits in the past 4 years at the balance sheet date and the discount rate of 1,7% (2017: 2%).

32. Non-current liabilities arising from purchase of shares

Non-current liabilities in the amount of HRK 8,131,049 relate to liabilities arising from the put/call option contracted at acquisition (Note 41), whereby the Group has the option of purchasing shares of the subsidiary PET currently held by the seller.

33. Non-current liabilities

	31 December 2018	31 December 2017
	HRK	*HRK*
Lease liabilities	1,194,409	1,677,234
	1,194,409	**1,677,234**
Bank borrowings		
Raiffeisenbank Austria d.d., Zagreb	22,252,725	22,540,944
Raiffeisenbank Austria d.d., Zagreb	12,515,683	21,129,645
Less: Current portion	(9,734,584)	(8,451,858)
	25,033,824	**35,218,731**
	26,228,233	**36,895,965**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Non-current liabilities to banks relate to two foreign currency borrowings from Raiffeisenbank Austria d.d.

The borrowing amounting to EUR 3,000,000.00 was granted in June 2017, with a fixed interest rate of 2.05% p.a. used to finance the 74% share in the company Power Engineering Transformatory Sp. z.o.o., Poland. Security instruments are 2 blank bills of exchange with bill of exchange statement, 1 general debenture of EUR 3,000,000.00, pledge over Company property and movables based on the Security Agreement amounting to EUR 25,000,000.00.

The second borrowing was granted in December 2017 in the amount of EUR 3,093,385.39 with a fixed interest rate of 1.85% p.a. used to refinance the long-term foreign currency borrowing at RBA d.d. granted in August 2016 in the amount of EUR 4,499,469.64, which was used to refinance the borrowing from HBOR's lending programme for the development of economic activities for financing the investment called High-Voltage Laboratory. Security instruments are 4 blank bills of exchange with bill of exchange statement, 1 general debenture of EUR 4,500,000.00, pledge over Company property and movables based on the Security Agreement amounting to EUR 25,000,000.00.
Furthermore, the Company contracted certain covenants for these borrowings, the most important of which are as follows:

- direct 60% of all domestic currency payment and a minimum of EUR 10,000,000.00 foreign currency payments through RBA accounts
- enable the bank to continuously monitor the use of pledged properties.
- The bank has a right to cancel the loan and to call it as due in the following cases:
  - late payment of any cash obligation under the contract
  - misuse of the borrowing or part of the borrowing
  - in the event that it does not partially or fully meet or partially violates any of the special contracted terms
  - in the event of material adverse change in the business, assets, liabilities or financial position of the Company
  - in the event that security instruments are no longer sufficient for the bank for any reason, and the Company does not offer another security instrument, suitable for the bank.

Movements in liabilities to banks and other financial institutions during the year can be summarised as follows:

	HRK
1 January 2017	**21,253,771**
Acquisition	1,677,234
New borrowings	22,213,581
Foreign exchange differences	203,237
Less: Current portion	(8,451,858)
31 December 2017	**36,895,965**
1 January 2018	**36,895,965**
Foreign exchange differences	(179,014)
Less: current portion	(754,134)
Less: Current portion of borrowings	(9,734,584)
31 December 2018	**26,228,233**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Long-term bank borrowings mature as follows:

	31 December 2018	31 December 2017
	HRK	*HRK*
From 1 to 2 years	7,547,804	10,627,834
From 2 to 3 years	3,337,880	7,619,678
From 3 to 4 years	2,825,392	3,151,554
From 4 to 5 years	2,781,591	2,817,618
Due in more than 5 years	9,735,566	12,679,281
	26,228,233	**36,895,965**

34. Liabilities to related parties

	31 December 2018	31 December 2017
	HRK	*HRK*
Končar Group companies:		
Končar - Electrical Industry Inc., Zagreb	1,394,356	1,277,422
Končar - Infrastructure and Services Ltd., Zagreb	1,006,257	868,297
Končar - Electrical Engineering Institute Inc, Zagreb	508,416	593,033
Končar - Switchgear Inc., Zagreb	341,385	2,125
Končar - Electronics and Informatics, Inc., Zagreb	97,545	129,983
Končar - Small Electrical Machines Inc, Zagreb	51,275	124,315
Končar - Instrument Transformers Inc., Zagreb	23,670	62,696
Končar - Steel Structures Inc., Zagreb	23,250	-
Končar - Power Plant and Electric Traction Engineering Inc. Zagreb	1,289	35,784
	3,447,443	**3,093,655**
Associates:		
Elkakon Ltd., Zagreb	4,712,212	3,582,824
Končar - Power Transformers, Ltd., Zagreb	74,000	19,991
	4,786,212	**3,602,815**
	8,233,655	**6,696,470**

As at 31 December, the ageing structure of liabilities to related parties was as follows:

	Total	Not past due	Past due				
			< 60 days	60-90 days	90-180 days	180-365 days	> 365 days
	HRK	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*
2018	**8,233,655**	7,070,584	1,163,071	-	-	-	-
2017	**6,696,470**	6,443,567	252,903	-	-	-	-

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

35. Current liabilities

	31 December 2018	31 December 2017
	HRK	*HRK*
Short-term borrowings		
Current portion of long-term borrowing (Note 33)	9,734,584	8,451,858
Short-term borrowings	8,410,716	-
Acquisition - borrowing from the company UTECH	528,395	551,193
	18,673,695	**9,003,051**
Current portion of lease liabilities (Note 33)	754,134	611,525
	754,134	**611,525**
	19,427,829	**9,614,576**

Movements in liabilities during the year can be summarised as follows:

	HRK
1 January 2017	**8,501,508**
Repayment of lease	(597,135)
Repayment of borrowings	(9,017,784)
New borrowings	1,139,202
Foreign exchange differences	(25,791)
Plus: Current portion	9,614,576
31 December 2017	**9,614,576**
Repayment of lease	(564,810)
Repayment of borrowings	(8,340,195)
New borrowings	8,483,832
Foreign exchange differences	499,842
Plus: Current portion	9,734,584
31 December 2018	**19,427,829**

The fair value of current borrowings does not differ significantly from its carrying value due to the short-term nature of these liabilities.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

36. Trade payables

	31 December 2018	31 December 2017
	HRK	*HRK*
Domestic trade payables	31,876,726	18,190,700
Foreign trade payables	70,945,748	51,160,038
	102,822,474	**69,350,738**

As at 31 December, the ageing structure of trade payables was as follows:

	Total	Not past due	Past due				
			< 60 days	60-90 days	90-180 days	180-365 days	> 365 days
	HRK	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*	*HRK*
2018	**102,822,474**	93,604,867	8,345,201	826,677	45,729	-	-
2017	**69,350,738**	68,318,806	1,005,843	2,350	19,808	3,931	-

37. Other short-term liabilities

	31 December 2018	31 December 2017
	HRK	*HRK*
Liabilities to employees		
Net salaries payable	6,894,045	6,436,037
	6,894,045	**6,436,037**
Taxes, contributions and similar charges		
Contributions, taxes and surtaxes payable	8,789,896	7,980,570
Income tax payable	21,237	686,238
VAT payable	1,632,618	336,786
	10,443,751	**9,003,594**
Other liabilities		
Sick leave liability, deductions etc.	85,551	83,487
Interest payable	182,964	131,251
Other liabilities	276,765	305,793
	545,280	**520,531**
Liabilities for distribution of profit	**150,437**	**101,616**
	18,033,513	**16,061,778**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

38. Accrued expenses and deferred income

	31 December 2018	31 December 2017
	HRK	*HRK*
Uninvoiced agent commissions	-	2,677,103
Deferred income	671,011	669,691
Other accrued expenses	234,726	5,006
Income from the right-to-use land	1,171,947	1,241,045
	2,077,684	**4,592,845**

39. Current provisions

	Warranty provisions	Other short-term provisions	Total
	HRK	*HRK*	*HRK*
1 January 2017	**41,077,135**	**3,062,752**	**44,139,887**
Additional provisions	-	1,400,642	1,400,642
Transfer from non-current provisions	3,694,695	-	3,694,695
31 December 2017	**44,771,830**	**4,463,394**	**49,235,224**
Additional provisions	963,304	53,810	1,017,114
Foreign exchange differences	(49,037)	-	(49,037)
Transfer from non-current liabilities	5,166,887	-	5,166,887
31 December 2018	**50,852,984**	**4,517,204**	**55,370,188**

40. Off-balance-sheet items

As at 31 December, the Group has the following off-balance sheet items:

	31 December 2018	31 December 2017
	HRK	*HRK*
Guarantees		
- in foreign currency	271,419,431	190,967,153
- in HRK	8,440,327	6,182,794
	279,859,758	**197,149,947**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

41. Business combinations

In May 2017, the Group acquired a 74% share in the company Power Engineering Transformatory Sp. z.o.o. (PET) from Czerwonak, Poznan, Poland. Since for the remaining 26% share there is a symmetric call and put option in effect in the period from 8 May 2020 until 31 December 2037, which can be used at the prices defined in the contract, this acquisition by the Group was accounted for as if it had immediately acquired the 100% share, and it recognised the amount payable as per the put/call option as deferred and paid at the purchase price.

The fair value of identifiable assets and liabilities of the subsidiary Power Engineering Transformatory Sp. z.o.o. (PET) as at 8 May 2017 was as follows:

	8 May 2017
	HRK
Non-current intangible assets	8,581
Non-current tangible assets	22,070,850
Non-current receivables	62,645
Inventories	2,793,477
Current receivables	378,109
Cash	646,822
Prepaid expenses	74,648
Provisions	(677,972)
Non-current liabilities	(2,199,350)
Current liabilities	(4,999,888)
Accrued expenses and deferred income	(1,253,050)
Total identifiable assets	**16,904,872**
Non-current liabilities related to share purchase	(8,001,769)
Gain on bargain purchase	**8,903,103**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

42. Related party transactions

Parties are considered to be related if one party has the ability to control the other party, is under common control or exercises significant influence over the other party in making financial or operational decisions. The Group's principal activity includes performing related party activities, including the purchase of goods and services. The nature of services with related parties is based on arm's length conditions. In addition to companies within the Končar Group and associates, the Group's related parties are the Group's Management Board and Supervisory Board.

During 2018, the Group engaged in transactions with related parties and realised revenues and expenses based on the trade of products and services, which can be analysed as follows.

2018	Operating activities				
	Receivables	Liabilities	Advances received	Revenues	Expenses
	HRK'000	*HRK'000*	*HRK'000*	*HRK'000*	*HRK'000*
Končar Group companies:					
Končar- Electrical Industry Inc.		1,394		-	5,590
Končar - Power Plant and Electric Traction Engineering Inc.	9,149	1	36	28,876	80
Končar - Infrastructure and Services Inc., Zagreb	-	1,006	-	65	1,970
Končar - Electrical Engineering Institute Inc.	28	509	-	117	4,315
Končar - Electronics and Informatics, Inc.	219	98	-	245	1,403
Končar - Small Electrical Machines, Inc., Zagreb	-	51	-	-	2,775
Končar - Instrument Transformers Inc.	1	24	-	34	1,037
Končar - Switchgear Inc.	824	341	-	2,877	562
Končar - Household Appliances Ltd.	-	-	-	-	1
Končar - Electric Vehicles Inc.	13	-	-	136	
Končar - Generators and Motors Inc.	-	-	-	-	88
Končar - Low Voltage Switches and Circuit Brakers Inc..	-	-	-	-	157
Končar-Engineering Co. for Plant Installation & Comnissioning Inc.	-	-	-	-	-
Končar Steel Structures Inc.	-	23	-	-	186
	10,234	**3,447**	**36**	**32,350**	**18,164**
Elkakon d.o.o., Zagreb	7,432	4,712	-	31,750	39,077
Končar - Power Transformers Ltd.	266	74	-	829	59
	7,698	**4,786**	**-**	**32,579**	**39,136**
	17,932	**8,233**	**36**	**64,929**	**57,300**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

During 2017, the Group engaged in transactions with related parties and realised revenues and expenses based on the trade of products and services, which can be analysed as follows.

2017	Operating activities				
	Receivables	Liabilities	Advances received	Revenues	Expenses
	HRK'000	*HRK'000*	*HRK'000*	*HRK'000*	*HRK'000*
Končar Group companies:					
Končar- Electrical Industry Inc.	–	1,278	–	-	6,101
Končar - Power Plant and Electric Traction Engineering Inc.	28,469	36	118	54,608	-
Končar - Infrastructure and Services Inc., Zagreb	-	868	-	129	1,908
Končar - Electrical Engineering Institute Inc.	-	593	-	-	1,818
Končar - Electronics and Informatics, Inc.	-	130	-	6	543
Končar - Small Electrical Machines, Inc., Zagreb	-	124	-	-	2,096
Končar - Instrument Transformers Inc.	1	63	-	17	1,282
Končar - Switchgear Inc. (previously: Končar - Medium Voltage Apparatus Inc., Zagreb).	-	2	-	-	10
Končar - Electric Vehicles Inc.	-	-	-	450	-
Končar - Switchgear Inc. from 29 December 2017 Končar - Switchgear Inc.)	688	-	-	1,442	429
Končar - Generators and Motors Inc.	-	-	-	8	29
Končar - Low Voltage Switches and Circuit Brakers Inc..	-	-	-	-	131
Končar-Engineering Co. for Plant Installation & Comissioning Inc.	-	-	-	51	-
Končar Steel Structures Inc.	-	-	-	-	171
	29,158	**3,094**	**118**	**56,711**	**14,518**
Associates:					
Elkakon Ltd., Zagreb	6,792	3,583	-	30,837	36,682
Končar - Power Transformers Ltd.	6,957	20	-	5,924	586
	13,749	**3,603**	**-**	**36,761**	**37,268**
	42,907	**6,697**	**118**	**93,472**	**51,786**

43. Financial instruments

In this note the following information will be disclosed:

A) The significance of financial instruments for the financial position and performance of the Group, and

B) The types and the nature of risks arising from financial instruments to which the Group is exposed at the end of the reporting period, and the method used by the Group in order to manage those risks.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

A) The significance of financial instruments for the financial position and performance of the Group

The significance of financial instruments for the financial position and performance of the Group is presented in the following tables:

31 December 2018

	Assets at amortised cost	Assets at fair value through P&L	Assets at fair value through OCI	**Total assets classified under**
	IFRS 9	*HRK'000*	*HRK'000*	*HRK'000*
Derivative financial assets - non-current	-	34	-	**34**
Available-for-sale financial assets	-	-	2,804	**2,804**
Derivative financial assets - current	-	293	-	**293**
Trade receivables	183,103	-	-	**183,103**
Receivables from related customers	17,932	-	-	**17,932**
Contract assets	8,161	-	-	**8,161**
Cash	103,778	-	-	**103,778**
	312,974	**327**	**2,804**	**316,105**

31 December 2017

	Assets at amortised cost	Assets at fair value through P&L	Assets at fair value through OCI	**Total assets classified under**
	HRK'000	*HRK'000*	*HRK'000*	*HRK'000*
Derivative financial assets - non-current	-	58	-	**58**
Available-for-sale financial assets	-	-	2,804	**2,804**
Derivative financial assets - current	-	883	-	**883**
Trade receivables	113,416	-	-	**113,416**
Receivables from related customers	42,907	-	-	**42,907**
Cash	130,043	-	-	**130,043**
	286,366	**941**	**2,804**	**290,111**

All the Group's liabilities have been classified as "At amortised cost", except for derivative financial instruments as explained in the following text.

The Group manages its capital to ensure its ability to continue as a going concern while maximising the return to shareholders by optimising the debt to equity ratio.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

	31 December 2018	31 December 2017
	HRK	*HRK*
Debt (interest-bearing)		
Long-term borrowings	26,228,233	36,895,965
Short-term borrowings (including current portion of long-term borrowings)	19,427,829	9,614,576
Less: Cash and cash equivalents	**(103,777,825)**	**(130,043,399)**
Net debt	**(58,121,763)**	**(83,532,858)**
Total equity	328,164,604	306,285,969
Equity and net debt	**270,042,841**	**222,753,111**
Net debt-to-equity ratio	**-**	**-**

Fair value of financial assets and liabilities

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. The Group uses the following hierarchy for determining the fair value of financial instruments:

- level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities
- level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly
- Level 3: techniques which use inputs which have a significant effect in the recorded fair value that are not based on observable market data

31 December 2018	Level 1	Level 2	Level 3	Total
	HRK'000	*HRK'000*	*HRK'000*	*HRK'000*
Listed shares	39	-	-	39
Fair value of derivative financial instruments	-	328	-	328
Assets at fair value through OCI	-	-	2,765	2,765
	39	**328**	**2,765**	**3,132**
31 December 2017				
Listed shares	39	-	-	39
Fair value of derivative financial instruments	-	941	-	941
Available-for-sale financial assets (Note 22)	-	-	2,765	2,765
	39	**941**	**2,765**	**3,745**

The fair value of the Group's financial assets and liabilities approximates the carrying amounts of the Group's assets and liabilities.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Derivative financial instruments

The fair value of financial instruments that are not traded in an active market presented in level 2 is determined by using valuation techniques. These valuation techniques maximise the use of observable market data where it is available and rely as little as possible on entity-specific estimates.

In addition to investing in equity instruments, the Group used the following methods and assumptions in estimating the fair value of financial instruments:

Receivables and bank deposits

For assets that mature within 3 months, the carrying value approximates their fair value due to the short maturities of these instruments. For longer-term assets, the interest rate does not deviate significantly from the current market rates and, consequently, the fair value approximates the carrying value.

Borrowings

The fair value of current liabilities approximates their carrying value due to the short maturities of these instruments. The Management Board believes that their fair value is not materially different from their carrying value.

Other financial instruments

The Group's financial instruments not carried at fair value are trade receivables, other receivables, trade payables and other current liabilities. The historical carrying amounts of receivables and payables, including provisions, which are all subject to normal trade credit terms, approximate their fair values.

B) Risks arising from financial instruments

The Group's operations are exposed to the following financial risks: market risk (including currency risk, interest rate risk and other price risk), credit risk and liquidity risk.

1 Market risk

Market risk is the fluctuation risk of fair value or future cash flows of financial instruments resulting from changes in market prices. Market risk comprises three types of risk: foreign exchange risk, interest rate risk and other price risks.

There were no significant changes to the Group's exposure to market risk or the manner in which it manages and measures the risk.

a) Foreign currency risk management and hedge accounting

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

The Group is exposed to this risk through sales, purchase and loans stated in foreign currency which is not the Group's functional currency. Foreign currencies primarily exposed to risk are EUR, USD, SEK, MAD, CZK, CHF, NOK, PLN, RON, GBP and HUF.

The Group is, therefore, exposed to the risk that movements in exchange rates will affect both its net income and financial position, as expressed in HRK.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

The Group exposes itself to foreign currency risk through sales, purchasing, borrowings and depositing of funds denominated in foreign currencies. EUR is not considered a currency of significant risk and the Group does not hedge against it, as opposed to all other currencies where the Group hedges through forward contracts on the trade of currencies with banks.

The Group's foreign currency exposure arises from:

- highly probable forecast transactions (sales/purchases) denominated in foreign currencies;
- commitments denominated in foreign currencies; and
- monetary items (mainly trade receivables, trade payables and borrowings) denominated in foreign currencies.

The Group's policy is to hedge all material foreign exchange risk associated with highly probable forecast transactions, firm commitments and monetary items denominated in foreign currencies.

The Group's policy is to hedge the risk of changes in the relevant spot exchange rate.

Hedging instruments

The Group mainly uses forward contracts as well as swap foreign exchange contracts to hedge foreign exchange risk. All derivatives must be entered into with counterparties with a credit rating of A or A negative.

Extracts of effectiveness testing policies for currency risk

Strategy: Cash flow hedges of foreign currency exposure in highly probable forecast transactions.

Effectiveness testing policy for currency risk

Prospective effectiveness testing for cash flow hedges

Prospective effectiveness testing is performed at the inception of the hedge and at each reporting date. The hedge relationship is highly effective if the changes in fair value or cash flow of the hedged item that are attributable to the hedged risk are expected to be offset by the changes in fair value or cash flows of the hedging instrument.

Prospective effectiveness testing is performed by comparing the numerical effects of a shift in the exchange rate (for example, EUR/USD rate) on: the fair value of the hedged cash flows measured using a hypothetical derivative; and the fair value of the hedging instrument. Consistent with the Group's risk management policy, the hedged risk is defined as the risk of changes in the spot exchange rate. Changes in interest rates are excluded from the hedge relationship (for both the hedging instrument and the hedged forecast transaction) and do not affect the calculations of effectiveness. Only the spot component of the forward contract is included in the hedge relationship (that is, the forward points are excluded). At least three scenarios should be assessed, unless the re terms of the hedging instrument perfectly match the critical terms of the hedged item, in which case one scenario is sufficient.

Retrospective effectiveness testing for cash flow hedges

Retrospective effectiveness testing is performed at each reporting date using the dollar offset method on a cumulative basis. The hedge is demonstrated to be effective by comparing the cumulative change in the fair value of the hedged cash flows measured using a hypothetical derivative, and the fair value of the hedging instrument.

$$\textbf{Effectiveness} = \frac{\textbf{Cumulative change in fair value of hedging instrument}}{\textbf{Cumulative change in fair value of hedged item (hypothetical derivative)}}$$

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

The change in the fair value of the spot component of the hedging instrument (the forward contract) is the difference between the fair value of the spot component at the inception of the hedge and at the end of the testing period. The difference is derived based on translating the foreign exchange leg of the forward contract at the current spot rate and discounting the net cash flows on the derivative using the zero-coupon rates curve derived from the swap yield curve.

The change in the fair value of the hedged cash flows of the hedged item (hypothetical derivative) is the difference between the value of the hypothetical derivative at the inception of the hedge and at the end of the testing period. The difference is derived based on translating the foreign exchange leg of the hypothetical derivative at the current spot rate and discounting the net cash flows on the hypothetical derivative using the zero-coupon rates curve derived from the swap yield curve.

The Group's exposure to currency risk at the reporting date is as follows:

31 December 2018

(in thousands of HRK)	EUR	USD	MAD	SEK	CZK	CHF	GBP	PLN	HUF	NOK	Total foreign currencies	HRK	Total
Trade receivables and receivables from related parties	105,061	5	-	26,239	112	2,570	2,949	19,955	-	-	156,891	41,345	201,035
Derivative instruments	328	-	-	-	-	-	-	-	-	-	328	-	328
Cash and cash equivalents	45,651	4,828	242	4,468	107	1,062	1,253	1,784	1	247	59,643	44,135	103,778
Total assets	**151,040**	**4,833**	**242**	**30,707**	**219**	**3,632**	**4,202**	**21,739**	**1**	**247**	**216,862**	**88,279**	**305,141**
Trade and other payables	67,591	-	8	2,755	230	362	-	5,616	-	-	76,562	34,494	111,056
Financial liabilities	34,768	-	-	-	-	-	-	10,888	-	-	45,656	-	45,656
Total liabilities	**102,359**	**-**	**8**	**2,755**	**230**	**362**		**16,504**	**-**	**-**	**122,218**	**34,494**	**156,712**

31 December 2017

(in thousands of HRK)	EUR	USD	MAD	SEK	CZK	CHF	GBP	PLN	HUF	Total foreign currencies	HRK	Total
Trade receivables and receivables from related parties	87,055	85	91	7,959	-	245	-	4,161	-	99,596	56,727	156,323
Derivative instruments	940	-	-	-	-	-	-	-	-	940	-	940
Cash and cash equivalents	105,981	764	256	6,028	2,957	1,857	3	2,190	1	120,037	10,008	130,045
Total assets	**193,976**	**849**	**347**	**13,987**	**2,957**	**2,102**	**3**	**6,351**	**1**	**220,573**	**66,735**	**287,308**
Trade and other payables	47,275	708	8	2,326	-	171	-	672	-	51,160	24,887	76,047
Financial liabilities	51,672	-	-	-	-	-	-	2,840	-	54,512	-	54,512
Total liabilities	**98,929**	**708**	**8**	**2,326**	**-**	**171**	**-**	**3,512**	**-**	**105,672**	**24,887**	**130,559**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Sensitivity analysis

A (weakening)/strengthening of the HRK exchange rate in relation to the following currencies by the presented percentages at the reporting date would increase/(decrease) profit before tax by the following amounts:

			2018	2017
	% Change 2018	% Change 2017	Effect on profit before tax HRK'000	Effect on profit before tax HRK'000
EUR	(1)%	(1)%	(782)	(548)
USD	3%	(13)%	153	(18)
SEK	(5)%	(3)%	(1,516)	(371)
CZK	(2)%	5%	-	149
CHF	2%	(9)%	79	(166)
GBP	(3)%	(4)%	(130)	-
Other currencies	-	-	3	(17)

This analysis assumes that all other variables, interest rates especially, remain unchanged. Percentage of changes in exchange rates are determined on the average change in these currencies over the past 12 months.

A reverse proportional change of the HRK against the above currencies by the same average percentage changes at the reporting date would have had the equal but opposite effect on the profit before tax, provided that all other variables are held constant.

b) Interest rate risk

The Group is not exposed to interest rate risks because all loans are contracted with a fixed interest rate, there are no variable interest rates, while most of the assets are not interest bearing.

c) Other price risks

The Group is not exposed to other price risks related to financial instruments.

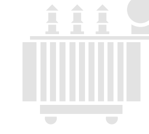
2) Credit risk

Credit risk refers to the risk that one party to a financial instrument will default on its contractual obligations resulting in financial loss to the other party. The Group has adopted a policy of only dealing with creditworthy counterparties and obtaining sufficient collateral, where appropriate, as a means of mitigating the risk of financial loss form defaults. The Group only transacts with entities with good credibility. The Group uses publicly available information on entities' financial position, reports on creditworthiness by independent credit rating agencies and its own trading records to rate its major customers. The Group's exposure and the credit ratings of its counterparties are continuously monitored and measured and the aggregate value of contracts concluded is spread amongst creditworthy counterparties.

A significant part of credit risk arises from trade receivables.

Trade and other receivables

The Group's exposure to credit risk is mainly affected by the individual characteristics of each customer. The demographics of the customer base, including the default risk of the industry and country, in which customers



Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

operate, has less of an influence on credit risk. The Group has established a credit policy under which each new customer is analysed individually for creditworthiness before standard payment and delivery terms and conditions are offered. The customers with insufficient creditworthiness are required to provide common payment collaterals, such bank letters of credit (L/C), bank collaterals, mortgages, debenture notes, bills of exchange, etc. The Group establishes an allowance for impairment that represents its estimate of incurred losses in respect of receivables.

The Group has not used derivative instruments to hedge these risks.

Impairment of financial assets

The Company has the following types of financial assets that are subject to the expected credit loss model:

- trade receivables for sales of goods and services
- contract assets
- debt instruments carried at amortised cost
- debt instruments carried at FVOCI

While cash and cash equivalents are also subject to the impairment requirements of IFRS 9, the identified impairment loss was immaterial.

Trade receivables and contract assets

The Group applies the simplified approach to measuring expected credit losses which uses a lifetime expected loss allowance for all trade and other receivables.

To measure the expected credit losses, trade and other receivables have been grouped based on shared credit risk characteristics and the days past due. The contract assets relate to unbilled work in progress and have substantially the same risk characteristics as the trade receivables for the same types of contracts. The Group has therefore concluded that the expected loss rates for trade receivables are a reasonable approximation of the loss rates for the contract assets.

The expected loss rates are based on the payment profiles of sales over a period of 36 month before 31 December 2018 or 1 January 2018 respectively and the corresponding historical credit losses experienced within this period.

The historical loss rates are adjusted to reflect current and forward-looking information on macroeconomic factors affecting the ability of the customers to settle the receivables.

The Group has identified the GDP and the unemployment rate of the countries in which it sells its goods and services to be the most relevant factors, and accordingly adjusts the historical loss rates based on expected changes in these factors.

The impairment as at 31 December 2018 and 1 January 2018 for trade receivables and contract assets is as follows:

31.12.2018	Total	Not past due	Past due 1-60 days	Past due 61-90 days	Past due 91-180 days	Past due 181-365 days	Past due over 365 days
	HRK' 000	*HRK' 000*	*HRK' 000*	*HRK' 000*	*HRK' 000*	*HRK' 000*	*HRK' 000*
Trade receivables	183,102,787	145,387,136	27,119,704	8,546,887	748,839	532,040	**768,181**
Receivables from related parties	17,931,894	12,519,661	2,492,328	-	-	2,919,905	**-**
Default rate (0%-9%)	-	0.00	0.01	0.12	0.24	0.54	**8.97**
Expected credit losses	**20.991**	**5.108**	**2.716**	**2.140**	**-**	**11.027**	

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

The Group did not recognise additional impairment losses on assets at amortised cost and equity instruments at fair value through other comprehensive income, as the analysis found that they are not material for the financial statements as at 1 January 2018. The impairment has not changed the value of the equity instruments in the balance sheet since they are still carried at fair value.

Trade receivables and contract assets are written off when there is no reasonable expectations of recovery. Indicators that there is no reasonable expectation of recovery include, amongst others, the failure of a debtor to engage in a repayment plan with the group, and a failure to make contractual payments for a period of greater than one year.

3) Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet their financial obligations as they fall due or that it will face difficulties in meeting these obligations. Liquidity risk management is the responsibility of the Management Board, which has built a quality frame for monitoring short-, middle- and long-term financing and all liquidity risk requirements. The Group manages liquidity risk by continuously monitoring the anticipated and actual cash flow based on the maturity of financial assets and liabilities.

The following table presents the maturity of financial liabilities of the Group as at 31 December 2018 in accordance with contracted undiscounted payments:

31 December 2018	Contractual cash flows	Less than 1 month	1 - 3 months	3 - 12 months	2 - 5 years	Over 5 years
	HRK'000	*HRK'000*	*HRK'000*	*HRK'000*	*HRK'000*	*HRK'000*
Liabilities						
Current liabilities to related parties	8,234	7,396	838	-	-	-
Current trade and other payables	102,972	52,005	50,315	652	-	-
Long-term borrowings	27,917	-	-	-	20,767	7,150
Short-term borrowings	20,240	183	2,255	17,802		-
Total liabilities	**159,363**	**59,584**	**53,408**	**18,454**	**20,767**	**7,150**

The following table presents the maturity of financial liabilities of the Group as at 31 December 2017 in accordance with contracted undiscounted payments:

31 December 2017	Contractual cash flows	Less than 1 month	1 - 3 months	3 - 12 months	2 - 5 years	Over 5 years
	HRK'000	*HRK'000*	*HRK'000*	*HRK'000*	*HRK'000*	*HRK'000*
Liabilities						
Current liabilities to related parties	6,697	5,874	823	-	-	-
Current trade and other payables	69,443	31,143	37,313	987	-	-
Long-term borrowings	46,907	-	-	475	32,660	13,772
Short-term borrowings	10,532	131	2,323	8,078	-	-
Total liabilities	**133,579**	**37,148**	**40,459**	**9,540**	**32,660**	**13,772**

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

44. Events after the balance sheet date

After the reporting date and until the approval date of these financial statements, there were no events that could significantly affect the annual financial statements of the Group for 2018, and that should, consequently, be disclosed.

45. Accounting policies applicable until 1 January 2018

A. Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services in the ordinary course of the Group's activities. Revenue is shown net of value added tax, excise tax, estimated returns, rebates and discounts.

Sales of goods and products

Revenue from the sale of goods and own products is recognised when all the following conditions have been met:

- the Group has transferred all significant risks and benefits arising from the ownership of the goods or products to the buyer;
- the Grouo does not retain constant involvement in the control of the assets sold up to a point usually related with ownership nor does it have control over the sale of goods;
- the amount of income can be measured reliably;
- it is probable that the economic benefits associated with the transactions will flow to the Group; and
- the costs incurred or to be incurred on those transactions can be measured reliably.

Income from services is recognised in the accounting period in which the services are rendered, by reference to completion of the specific transaction assessed on the basis of the actual service provided as a proportion of the total services to be provided.

B. Financial assets and financial liabilities

Financial assets

Investments are recognised and derecognised on the trade date where the purchase or sale of a financial asset is under a contract whose terms require the delivery of the investment within the time frame established by the market concerned, and are initially measured at fair value, plus transaction costs, except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value.

Financial assets are classified into the following categories:

o 'Financial assets at fair value through profit or loss (FVTPL)'

Financial assets are classified as FVTPL where the financial asset is either held for trading or it is designated as FVTPL. Financial assets at FVTPL are stated at fair value, with any resultant gain or loss recognised in profit

or loss. All derivative financial instruments are included in this category, except if designated and effective as hedging instruments in which case hedge accounting is applied.

o 'Held-to-maturity investments'

Bills of exchange and promissory notes with fixed or determinable payments and fixed maturity dates that the Group has the positive intent and ability to hold to maturity are classified as held-to-maturity investments. Held-to-maturity investments are carried at amortised cost using the effective interest method less any impairment, with revenue recognised on an effective yield basis.

o 'Available-for-sale financial assets'

Financial assets available for sale are non-derivative financial assets which are designated as such or cannot be included in any of the above mentioned categories. These assets are stated at fair value. Gains and losses arising from changes in fair value are recognised in other comprehensive income in the investments revaluation reserve with the exception of impairment losses, interest calculated using the effective interest method and foreign exchange gains and losses on monetary assets, which are recognised directly in profit or loss. Where the investment is disposed of or is determined to be impaired, the cumulative gain or loss previously recognised in other comprehensive income in the investments revaluation reserve is included in profit or loss for the period.

o 'Loans and receivables'

Trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as loans and receivables. Loans and receivables are measured at amortised cost using the effective interest method, less any impairment. Interest income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

Impairment of financial assets

Financial assets, other than those at fair value through profit or loss, are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired if there is objective evidence of impairment resulting from one or more events that occurred after the initial recognition of an asset when the event affects the estimated future cash flows from the financial asset.

For certain categories of financial assets, such as trade receivables, assets that are assessed not to be impaired individually are subsequently assessed for impairment on a collective basis. Objective evidence of impairment for a portfolio of receivables could include the Group's past experience of collecting payments, an increase in the number of delayed payments in the portfolio past the average credit period of 60 days, as well as observable changes in national or local economic conditions that correlate with default on receivables.

Derecognition of financial assets

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Financial liabilities and equity instruments issued by the Group

Classification as debt or equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

Equity instruments

An equity instrument is any contract that provides evidence to a residual interest in the assets of the Group after deducting all of its liabilities. Equity instruments issued by the Group are recorded at the proceeds received, net of direct issue costs.

Share capital

a. Ordinary shares

Share capital represents the nominal value of shares issued.

The share premium includes the premium at the issuance of shares. Transaction costs directly attributable to the issue of ordinary shares are recognised as a deduction from equity.

b. Share capital repurchase

The amount paid for the repurchase of the share capital, including direct costs related to the repurchase, is recognised as an impairment within capital and reserves. Repurchased shares are classified as treasury shares and presented as a deduction from total capital and reserves.

Financial guarantee contract liabilities

Financial guarantee contract liabilities are measured initially at their fair values and are subsequently measured at the higher of:

- the amount of the obligation under the contract, as determined in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets; and
- the amount initially recognised less, where appropriate, cumulative amortisation recognised in accordance with the revenue recognition policies (dividend and interest revenue).

Financial liabilities at fair value through profit or loss

Financial liabilities are classified as "at fair value through profit or loss" where the financial liability is either held for trading or designated by the Group as "at fair value through profit or loss".

Financial liabilities at fair value through profit or loss are stated at fair value, with any resultant gain or loss recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any interest paid on the financial liability.

Other financial liabilities

Other financial liabilities, including borrowings, are initially measured at fair value, net of transaction costs.

Notes to the Consolidated Financial Statements

for the Year Ended 31 December 2018

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Derecognition of financial liabilities

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire. Financial risk management and disclosures in accordance with IFRS 7 are set out in Note 43 to these financial statements.

Publisher: Končar Distribution and Special Transformers, Inc.
Design & Prepress: Studio Prodomo d.o.o.

April 2019

Tradition. Knowledge. Responsibility.

KONČAR
Distribution and Special Transformers, Inc.
Mokrovićeva 8
P.O.Box 100
10090 Zagreb, Croatia
Phone: + 385 1 378 3713
Fax: + 385 1 379 4051
E-mail: info@koncar-dst.hr

www.koncar-dst.hr

Power Engineering Transformatory Sp. z o.o.
ul. Gdyńska 83, 62-004 Czerwonak, Polska
Tel.: +48 61 892 88 88
E-mail: info@petransformatory.pl
www.petransformatory.pl

357018 en IV2019