

T-HT GROUP
ANNUAL REPORT
ON THE STATUS AND BUSINESS OPERATIONS
OF THE COMPANY AND T-HT GROUP
FOR THE BUSINESS YEAR 2011

February 2012

T-HT GROUP

in HRK million	Jan-Dec 2011	Jan-Dec 2010	% of change A11/A10
Revenue	8,067	8,372	-3.6%
EBITDA before exceptional items	3,782	3,694	2.4%
Exceptional items	162	32	412.0%
EBITDA after exceptional items	3,619	3,662	-1.2%
EBIT (Operating profit)	2,205	2,246	-1.8%
Net profit after minority interest	1,811	1,831	-1.1%
EBITDA margin before exceptional items	46.9%	44.1%	2.8 p.p.
EBITDA margin after exceptional items	44.9%	43.7%	1.1 p.p.
EBIT margin	27.3%	26.8%	0.5 p.p.
Net profit margin	22.4%	21.9%	0.6 p.p.
Balance Sheet	At 31 Dec 2011	At 31 Dec 2010	% of change A11/A10
Total non current assets	7,461	8,008	-6.8%
Total current assets	5,675	5,521	2.8%
TOTAL ASSETS	13,136	13,529	-2.9%
Total issued capital and reserves	11,019	11,054	-0.3%
Total non current liabilities	303	336	-9.9%
Total current liabilities	1,814	2,139	-15.2%
TOTAL EQUITY AND LIABILITIES	13,136	13,529	-2.9%
Cash flow	Jan-Dec 2011	Jan-Dec 2010	% of change A11/A10
Net cash flow from operating activities	2,988	3,266	-8.5%
Net cash flow from investing activities	-696	-1,389	49.8%
Net cash flow from financing activities	-1,874	-2,792	32.9%
Net increase/decrease in cash and cash equiv.	422	-912	146.2%
Cash and cash equivalents at the end of period	3,704	3,282	12.9%
CAPEX	877	1,153	-23.9%
CAPEX / Revenue ratio	10.9%	13.8%	-2.9 p.p.
	At 31 Dec 2011	At 31 Dec 2010	% of change A11/A10
ROE	16.4%	15.9%	0.5 p.p.
ROCE	19.5%	19.7%	-0.3 p.p.
Number of employees (FTEs)	6,032	6,322	-4.6%

OPERATIONAL HIGHLIGHTS

Key operational data	Jan-Dec 2011	Jan-Dec 2010	% of change A11/A10
Mobile subscribers in 000			
Number of subscribers	2,418	2,437	-0.8%
- Residential	1,964	2,003	-1.9%
- Business	454	435	4.4%
Number of postpaid subscribers	1,035	1,003	3.2%
- Residential	581	568	2.3%
- Business	454	435	4.4%
Number of prepaid subscribers ³⁾	1,383	1,434	-3.6%
Minutes of use (MOU) per average subscriber	134	136	-1.2%
- Residential	100	100	0.7%
- Business	285	300	-5.0%
Blended ARPU (monthly average for the year in HRK)²⁾	94	104	-10.0%
- Residential	74	83	-11.0%
- Business	184	202	-8.9%
Blended non-voice ARPU (monthly average for the year in HRK)²⁾	23	25	-7.3%
SAC per gross add in HRK	122	160	-23.7%
Churn rate (%)	2.7	2.5	0.2 p.p.
Penetration (%) ¹⁾	119.9	117.8	2.1 p.p.
Market share of subscribers (%) ¹⁾	47.0	46.7	0.3 p.p.

¹⁾ Source: published VIPnet's quarterly report for 3Q 2011 and Tele2's quarterly report for 4Q 2010 and 2011. Number of subscribers for VIPnet for 4Q 2011 are internally estimated.

²⁾ Due to T-Mobile and T-Com merger and within the new segmental reporting explained above, as of Q1 2011 calculation of ARPU was changed to show consolidated mobile revenues rather than unconsolidated mobile revenues.

³⁾ In September 2011 definition of prepaid subscribers has been changed in order to be aligned with HAKOM definition. According to new definition, only SIM's with traffic or voucher recharge in the last 90 days should be considered as the subscribers. Previous year has been restated with all related KPIs to be aligned with new definition.

Key operational data	Jan-Dec 2011	Jan-Dec 2010	% of change A11/A10
Fixed mainlines in 000			
Total mainlines¹⁾	1,267	1,438	-11.9%
- Residential	1,074	1,220	-12.0%
- Business	193	217	-11.4%
Total Traffic (mill. of minutes)	2,790	3,177	-12.2%
- Residential	2,083	2,320	-10.2%
- Business	706	856	-17.5%
ARPA voice per access (monthly average for the year in HRK)	121	131	-7.3%
- Residential	101	107	-5.7%
- Business	238	264	-10.0%
IP mainlines/customers in 000			
ADSL mainlines	651	629	3.4%
- Residential	539	524	2.9%
- Business	112	105	6.0%
TV customers²⁾	341	303	12.3%
- Residential	321	286	12.3%
- Business	19	17	12.4%
Fixed-line customers	1	1	5.1%
VPN connection points	4	4	10.0%
ADSL mainlines ARPA (monthly average for the year in HRK)	123	127	-3.1%
- Residential	120	124	-3.1%
- Business	134	138	-2.5%
Data lines in 000			
Total data lines	5	6	-6.7%
Wholesale customers in 000			
CPS (Carrier Pre-Selection)	96	221	-56.5%
NP (Number portability) users/number	514	416	23.5%
ULL (Unbundled Local Loop)	148	133	11.7%
WLR (Wholesale Line Rental) ³⁾	124	0	-

¹⁾ Includes POTS+FGSM+ ISDN+Payphones

²⁾ Includes IPTV, DTH and Cable TV customers

³⁾ On July 1st HT published new WLR (Wholesale Line Rental) offer according to HAKOM regulation

Presentation of information in the Annual Report

Unless the context otherwise requires, references in this publication to "T-HT Group" or "the Group" or "T-HT" are to the Company - Hrvatski Telekom d.d., together with its subsidiaries.

References to "HT" or the "Company" are to the Company - Hrvatski Telekom d.d.

References to "Iskon" are to the Company's wholly-owned subsidiary, Iskon Internet d.d.

References to "Combis" are to the Company's wholly-owned subsidiary, Combis, usluge integracije informatičkih tehnologija d.o.o.

References in this publication to "Agency" are to the Croatian National Regulatory Authority, the Agency for Post and Electronic Communications.

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1. INTRODUCTION

1.1. Corporate Profile

At a Glance

The T-HT Group is the leading provider of telecommunications services in Croatia, offering fixed and mobile telephony services as well as wholesale, Internet, data and ICT services. As of 1 January 2010, the Group conducts its business through its Residential and Business units.

The basic activities of Hrvatski Telekom d.d. and subsidiary companies comprise the provision of electronic communications services and the design and construction of electronic communications networks within the Republic of Croatia. In addition to the provision of fixed telephony lines services (fixed telephony line access and traffic, as well as fixed network supplementary services), the Group also provides Internet services and ICT services, data transmission services (lease of lines, Metro-Ethernet, IP/MPLS, ATM), operating with GSM and UMTS mobile telephone networks.

History and Incorporation

Hrvatski Telekom d.d. (HT d.d. or the Company) is a joint stock company majority owned by Deutsche Telekom AG (DTAG). It was incorporated on 28 December 1998 in the Republic of Croatia, pursuant to the provisions of the Act on the Separation of Croatian Post and Telecommunications into Croatian Post and Croatian Telecommunications, by which the business operation of the former HPT - Hrvatska pošta i telekomunikacije (HPT s.p.o.) was separated and transferred into two new joint stock companies, HT - Hrvatske telekomunikacije d.d. (HT d.d.) and HP - Hrvatska pošta d.d. (HP d.d.). The Company commenced its operations on 1 January 1999.

Pursuant to the terms of the Law on Privatization of Hrvatske telekomunikacije d.d. (Official Gazette No. 65/99 and No. 68/01), on 5 October 1999, the Republic of Croatia sold a 35% share in HT d.d. to DTAG, and on 25 October 2001 DTAG purchased a further 16% share in HT d.d. and thus became the majority shareholder with a 51% share in ownership. As of 17 February 2005, the Government of the Republic of Croatia transferred 7% of its shares in HT d.d. to the Fund for Croatian Homeland War Veterans and Their Families, pursuant to the Law on Privatization of HT d.d. (Official Gazette No. 65/99 and 8/2001).

In 2002, HT mobilne komunikacije d.o.o. (HTmobile) was established as a separate legal entity and subsidiary wholly owned by HT d.d. for the provision of mobile telecommunication services. HTmobile commenced its commercial activities on 1 January 2003 and in October 2004, the company name was officially changed to T-Mobile Croatia d.o.o. (T-Mobile). On 1 October 2004, the Company was re-branded as T-HT, thus becoming a part of the global „T“ family of Deutsche Telekom. The change of identity at corporate level was followed by the creation of trade marks for the two separate business units of the Group: the fixed network operations business unit, T-Com, which also provided wholesale, Internet and data services, and the mobile operations business unit, T-Mobile.

In May 2006, the Group acquired 100% of shares of Iskon Internet d.d., one of the leading alternative telecom providers in Croatia.

Pursuant to the provisions of the Law on Privatization of HT d.d. (Official Gazette No. 65/99 and No. 68/01), on 5 October 2007, the Republic of Croatia sold 32.5% of T-HT ordinary shares by Initial Public Offering (IPO). Of the 32.5% of shares, 25% were sold to Croatian retail investors, while 7.5% were distributed among Croatian and international institutional investors.

Following the sale of shares to present and former employees of Hrvatski Telekom and Croatian Post in June 2008, the Government of the Republic of Croatia reduced its holding from 9.5% to 3.5%, while private and institutional investors held 38.5%.

In October 2009, an agreement was signed by which T-Mobile Croatia was merged into HT d.d. The merger came into effect on 1 January 2010, after which time the Group was organised into Residential and Business units. In addition the Company's registered name was officially changed from HT - Hrvatske telekomunikacije d.d. to Hrvatski Telekom d.d. on 21 May 2010.

On 17 May 2010 HT d.d. has completed the acquisition of the IT services company Combis d.o.o., extending its reach into the provision of IT software and services for a client base that ranges from small businesses to government departments. In December 2010, according to records held at the Central Depository and Clearing Company, the Republic of Croatia transferred 2,859,148 shares of Hrvatski Telekom d.d., equal to 3.5% of the entire share capital of the Company, to the owner account of the Pensioners' Fund. Following this transfer, the Republic of Croatia no longer holds shares of Hrvatski Telekom d.d.

1.2. Investor Information

Economic environment and share price performance

Global uncertainties and market volatility prevailed in 2011, with growing budget deficits, the Eurozone debt crisis, an overall fall in consumer confidence, social unrest and a slowdown in the economies of Asia and South America, among others. These factors reignited concerns about a prolonged global recession. Uncertainty was further exacerbated by the Japanese tsunami, the Arab Spring and other tensions in the Middle East, with the latter triggering concerns about global oil supplies and inflation.

Global markets were highly volatile and largely subdued. In August, Standard & Poor's removed for the first time the AAA credit rating of US, and this prompted further downward pressure on stock markets worldwide.

With Croatia's parliamentary election scheduled for December 2011, the long overdue fiscal consolidation and structural reforms of Croatia's economy were postponed. Domestic consumption hit a new low, unemployment remained high and problems with overdue payments persisted. These factors caused analysts to downgrade Croatia's 2011 GDP growth forecast throughout the year to settle at around zero.

Big policy initiatives from the newly elected left-of-centre coalition Government are yet to emerge. The major credit agencies are expected to visit Croatia in first half of 2012 to discuss the sovereign credit rating. Meanwhile, in January 2011 a referendum on EU membership showed majority support and the accession target date is 1 July 2013.

Against the economic backdrop outlined above and poor liquidity, the Zagreb Stock Exchange experienced strong downward pressure, especially in the second half of the year, amid speculation that a dividend tax would be introduced. Consequently, the benchmark CROBEX index fell 17.6% in 2011, after two years of growth. Annual trading volumes showed another year of decline, falling 9.4%.

T-HT shares ended the year at HRK 242.00, down 16.2% on the HRK 288.71 closing price at the end of 2010 and marginally outperforming the CROBEX. The price decline was primarily seen in the first half of the year following the Company's dividend announcement in mid February and ex-dividend date in early May. The year's highest price was HRK 315.99, the lowest being HRK 224.05 (Source: Zagreb Stock Exchange).

In 2011, T-HT shares underperformed the Dow Jones Euro Stoxx Telecommunications Index (a leading indicator of the telecommunications industry that measures the performance of some Europe's largest telecom companies) by 10 percentage points, having outperformed it for the previous two years.

*T-HT Share and GDR as compared to CROBEX and Dow Jones Europe Stoxx Telecommunications Index
1 January 2011 - 31 December 2011*



Although its turnover was around 15% lower than in 2010, T-HT was once again the most traded share on the Zagreb Stock Exchange, with HRK 1.3 billion of turnover, accounting for 24.1% of the ZSE's total trade by value of shares in 2011 (2010: HRK 1.5 billion, 25.8%).

As at 31 December 2011, T-HT was the second largest company on ZSE, with a market capitalisation HRK 19.8 billion (EUR 2.63 billion) representing 15.2% of the total market capitalization by value (Source: Zagreb Stock Exchange).

At the last revision of the CROBEX index, T-HT's weighting was set at 15% of the index.

Besides T-HT shares being listed on the Official Market of the Zagreb Stock Exchange, Global Depositary Receipts (GDRs), each representing one T-HT Share, are traded on London Stock Exchange.

In October, at the 21st annual conference of the Zagreb Stock Exchange, T-HT accepted the second place award for Investor Relations in Croatia 2011 sponsored by popular business newspaper Poslovni dnevnik (2010: first place award for best IR).

Dividend policy

The Dividend policy of the Company was set out in the prospectus that accompanied its Initial Public Offering in October 2007:

The future dividend policy should be that any dividends declared and paid in respect of any year following the year in which Offering takes place, shall range from 50% to 100% of the Company's distributable profits earned in the immediately preceding year. Any annual dividend shall depend on the overall financial position of the Company and its working capital needs at the relevant time (including but not limited to the Company's business prospects, cash requirements, financial performance, and other factors including tax and regulatory

considerations, payment practices of other European telecommunications operators and general economic climate).

Dividend for the 2010 financial year

On 4 May 2011, the General Assembly of the Company approved a dividend payment to shareholders of HRK 1,863,783,056.60 (HRK 22.76 per share), representing a dividend payout ratio of 100%. The dividend was paid in second half of May 2011.

At the end of 2011, this represented a dividend yield of 9.4% on T-HT's closing price of HRK 242.00. Using the average closing share price over 2011, HRK 265.56, the dividend yield was 8.6%.

Dividend proposal for the 2011 financial year

The Management Board and Supervisory Board of Hrvatski Telekom d.d. propose to this year's General Assembly, to be held on April 25, the distribution of a dividend of HRK 22.14 per share which will be paid from 2011 financial year profit, resulting in total dividend payment of HRK 1,813,012,164.90.

The Supervisory Board gave its consent to the Management Board to pay to the shareholders an advance dividend of HRK 11.07 per share or HRK 906,506,082.45 in total.

The date on which shareholder acquires the right to advance dividend payment amount, is established as 20 February 2012 and the due date for advance dividend payment is 27 February 2012.

According to the proposal, the date on which shareholder acquires the right to residual dividend amount of HRK 11.07 per share is 25 April 2012, the day of the General Assembly session. The residual amount will be paid to shareholders on 21 May 2012.

Shareholder Structure as at 31 December 2011

Deutsche Telekom	51.0%
War Veterans' Fund	7.0%
Raiffeisen Mandatory Pension Fund*	5.3%
Pensioners' Fund	3.5%
Private and other institutional investors	33.2%

* Excludes possible GDR holdings

Total number of shares issued: 81,888,535

Deutsche Telekom remains the majority shareholder with a 51% holding, while the Croatian War Veterans' Fund continues to own 7%. In November 2010 the Republic of Croatia transferred its 3.5% holding to the Pensioners' Fund.

In April 2011 the Company received notification from Raiffeisen Mandatory Pension Fund Management Company Plc that Raiffeisen Mandatory Pension Fund has exceeded the 5% threshold in HT d.d. According to Central Depository & Clearing Company web site at the end of 2011, it held 5.3% of T-HT shares.

The remaining 33.2% is in private and other institutional hands, with more than 220,000 Croatian private investors holding T-HT shares representing 23.3% of the total share capital of the Company.

Financial Calendar	Date
Release of full year 2011 results	February 14, 2012
The General Assembly of the Company	April 25, 2012
Release of first quarter 2012 results	April 30, 2012
Release of first half 2012 results	July 30, 2012
Release of first nine months 2012 results	October 30, 2012

The above-mentioned dates are subject to change

General information on Shares and GDRs

Shares:	ISIN: HRHT00RA0005
Regulation S GDRs:	ISIN: US44330H2004
Rule 144A GDRs:	ISIN: US44330H1014
ZSE Share trading symbol:	HT-R-A
LSE GDR trading symbol:	THTC
Portal Rule 144A GDR listing symbol:	P443296108
Reuters:	THTC.L, HT.ZA
Bloomberg:	THTC LI, HTRA CZ
Number of Shares:	81,888,535
Type:	Ordinary share
Nominal value:	HRK 100

Each GDR represents one Share on deposit with the Custodian.

The depository for the GDR is:

JPMorgan Chase Bank, N.A.,
1 Chase Manhattan Plaza, Floor 21
New York
New York, 10005-1401
United States of America

The Custodian is:

Privredna Banka Zagreb
Račkoga 6
10000 Zagreb
Croatia

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1.3. Management Board

IVICA MUDRINIĆ

President of the Management Board and CEO

Ivica Mudrinić was born in 1955. He graduated in electrical engineering from the University of Toronto in 1978. His first job was in the Product Development Department of Motorola Communications, and in 1985 he founded his own company, MX Engineering Inc. In 1990, he returned to Croatia and soon became adviser for communications to the President of the Republic. At the end of the following year, he became Assistant Minister for Maritime Affairs, Transportation and Communications, and in 1992 was appointed Minister. From 1994 Ivica Mudrinić also served as President of the Telecommunications Council. He held the post of President of the Management Board of Hrvatska radiotelevizija (Croatian Radio and Television) from 1996 until 15 October 1998, when he was appointed General Manager of Hrvatska pošta i telekomunikacije (Croatian Post and Telecommunications). Since the separation of Croatian Post and Telecommunications on 1 January 1999, he has served as President of the Management Board of Hrvatski Telekom.

DINO IVAN DOGAN

Member of the Management Board

Chief Financial Officer

Born in 1963, completed the Study 'Business Administration (technical oriented)', University of Stuttgart, in 1988. Dino Ivan Dogan brings considerable experience of the telecommunications industry, having served as Chief Financial Officer and Member of the Board at Mobilkom Austria AG since August 2009. In 2010, he also assumed the role of Chief Integration Officer for Mobilkom Austria AG's merger with Telekom Austria AG. Prior to joining Mobilkom Austria AG, Dr. Dogan was Chief Financial Officer and Member of the Board of its subsidiary, the Croatian mobile operator VIPnet, a post he held from July 2003 to July 2009, after spending 10 years in managerial positions at Alcatel. From 1 April 2011 on, he will hold the position of Member of the Management Board and Chief Financial Officer of Hrvatski Telekom.

IRENA JOLIĆ ŠIMOVIĆ

Member of the Management Board

Chief Operating Officer, Business

Irena Jolić Šimović was born in 1969. She graduated from the Faculty of Economics in Zagreb and received an MBA from IEDC, Bled, Slovenia. Prior to joining Hrvatski Telekom in 1998, she worked at Croatian Radio and Television (HRT), the Ministry of the Sea, Transport and Communications and the Ministry of Immigration. She was Executive Director for Corporate Strategy and Business Development until August 2006, when she was appointed Member of T-HT's Management Board and Chief Human Resources Officer. Irena Jolić Šimović was Chief Operating Officer T-Com from October 2008 until December 2009. Following the Group's restructuring in January 2010, she became Chief Operating Officer Business with responsibility for Sales, Marketing, Customer Service, Wholesale and ICT Business Solutions. In March 2010, Irena Jolić Šimović was honoured as one of the World Economic Forum's Young Global Leaders 2010, a unique community of exceptional young leaders who share a commitment to shaping the global future.

JOHAN H.M. BUSÉ

Member of the Management Board

Chief Operating Officer, Residential

Johan Busé was born in 1969. After completing the study of economics, he started his career in retail marketing at British Petroleum in Belgium and the Netherlands, joining T-Mobile in 2000, where he took the position of the Head of Business Development. After that he led several marketing departments of T-Mobile in the Netherlands, Germany, and Croatia. From 2006 to 2008 he held the position of the Member of the Management Board and Chief Marketing Officer of T-Mobile Croatia. He then joined the Indonesian mobile operator AXIS as Chief Marketing Officer, helping it to become the fastest growing 3G operator in Indonesia. On 1 April 2010 Mr. Busé returned to HT when he was appointed Member of the Management Board and Chief Operating Officer Residential, responsible for Sales, Marketing, and Customer services.

BRANKA SKARAMUČA**Member of the Management Board****Chief Human Resources Officer**

Branka Skaramuča was born in 1958 and in 1982 obtained a master's degree in Psychology at the Faculty of Philosophy, University of Zagreb. She began her career with the pharmaceutical company PLIVA in 1985, where she worked in Human resources. In 1989 she was appointed Head of Marketing Communications in part of its FMCG portfolio, being promoted to the position of HR Director for Croatia in 1993 and then becoming Global HR Director until February 2002. She joined Hrvatski Telekom in 2002 as a Member of the Management Board and Chief Human Resources Officer, becoming a Management Board member and Chief Human Resources Officer of T-Mobile Hrvatska in March 2004. In September 2008 the Supervisory Board of Hrvatski Telekom appointed Branka Skaramuča a Member of the Management Board and Chief Human Resources Officer of the T-HT Group.

BOŽIDAR POLDRUGAČ**Member of the Management Board****Chief Technical and Chief Information Officer**

Božidar Poldrugač was born in 1967. He graduated from the Faculty of Electrical Engineering and Computing, Zagreb University in 1992 and earned a master's degree from the same faculty in 2000. He began his career at Croatian Post & Telecommunications in 1993 and participated in all the development activities related to implementation of the first GSM network in Croatia. After the separation of Croatian Post & Telecommunications, he continued his career in Hrvatski Telekom, where he served as a Member of the Management Board and Director of Mobile Communications from October 1999 to October 2001. He was Chief Technical Officer for Mobile Communications at Hrvatski Telekom from October 2001 to January 2003, when the subsidiary company T-Mobile Croatia was launched. In March 2007, he was appointed Member of the Management Board and Chief Technical and Chief Information Officer for the T-HT Group.

JÜRGEN P. CZAPRAN**Member of the Management Board****Chief Financial Officer until March 31st 2011****Compensation to the Management Board members in 2011:**

In 2011, Ivica Mudrinić, President of the Management Board, was paid a fixed salary contracted in annual gross amount of HRK 2,120,500 in average net monthly installments of HRK 93,085. Variable part, in accordance with 2010 goals achievement, amounted to HRK 616,899 net. Payment according to MTIP 2008 amounted to HRK 222,909 net. Income in kind amounted to HRK 154,565 gross for company car usage.

Irena Jolić Šimović, member of the Management Board, was in 2011 paid a fixed salary contracted in gross amount of HRK 1,561,171 in average net monthly installments of HRK 68,379. Variable part, in accordance with 2010 goals achievement, amounted to HRK 243,956 net. Payment according to MTIP 2008 amounted to HRK 101,180 net. The income in kind amounted to HRK 139,679 gross for company car usage.

Johan Buse, member of the Management Board, was in 2011 paid a fixed and variable salary contracted in annual gross amount of HRK 2,578,961. The amount of income in kind was HRK 380,073 gross for rental, insurance and company car usage.

Božidar Poldrugač, member of the Management Board, was in 2011 paid a fixed salary contracted in annual gross amount of HRK 1,430,865 in average net monthly installments of HRK 65,741. Variable part, in accordance with 2010 goals achievement, amounted to HRK 290,223 net. Payment according to MTIP 2008 amounted to HRK 121,376 net. The income in kind amounted to HRK 157,378 for company car usage.

Jürgen P. Czapran, member of the Management Board until March 31st 2011, was in this period 2011 paid a fixed and variable salary contracted in annual gross amount of HRK 1,288,058. The amount of income in kind was HRK 172,184 gross for rental, insurance and company car usage.

Dino Ivan Dogan, member of the Management Board from April 1st 2011, was in 2011 paid a contracted fixed salary in gross amount of HRK 1,113,421, in average net monthly installments of HRK 73,806. Contracted sign-in bonus amounted to HRK 523,107 net. The income in kind amounted to HRK 87,693 gross for company car usage.

Branka Skaramuča, member of the Management Board, was in 2011 paid a fixed salary contracted in annual gross amount of HRK 1,379,016, in average net monthly installments of HRK 60,338. Variable part, in accordance with 2010 goals achievement, amounted to HRK 260,079 net. Payment according to MTIP 2008 amounted to HRK 113,126 net. The benefit in kind amounted to HRK 136,589 gross for company car usage.

Share-based payment transactions

Mid-term incentive plans (MTIPs) and long-term incentive plan (LTIP - Variable II) exist at HT level to ensure competitive total compensation for members of the Management Board, senior executives and other beneficiaries. The plans promote the medium and long-term value enhancement of the Company, thus aligning the interests of management and shareholders. First HT's MTIP is introduced in 2008.

MTIP is generally set up as a cash-based plan linked to two equally weighted, share-based performance parameters – one absolute and one relative. If both performance targets are achieved, then the total amount earmarked as an award to the beneficiaries by the respective employers is paid out; if one performance target is achieved, 50 percent of the amount is paid out, and if neither performance target is achieved, no payment is made.

In 2011 new cash-based long-term incentive plan LTIP - Variable II was established. Variable II includes four equally weighted performance parameters. In contrast to the former MTIP structure, Variable II offers the option of exceeding the amounts earmarked for award, limited to 150% of the award volume per parameter. The parameters are independent from each other, hence each parameter is assessed separately. Both potential excesses and shortfalls in relation to targets are accounted for on a graded basis per target parameter (departure from the principle of “all or nothing”).

As a result of the extension of the new LTIP – Variable II 2011 duration from three to four years, there appears a lack of payment after three years. In order to close the lack of a payout option, the Transitional HT MTIP 2011 is established. Transitional HT MTIP 2011 was set up as a “bridging instrument” before introducing newly designed four-year-term LTIP 2011 (Variable II).

All MTIPs cover period of three years and LTIP- Variable II covers period of four years. Upon expiry of the term of the plan (after three years for MTIP and after four years for LTIP- Variable II), the Supervisory Board of the Company shall determine for MTIP whether each of the targets has been achieved or for Variable II target achievement for each of four parameters. Based on the findings of the Supervisory Board, the Management Board shall determine and announce the level of target achievement.

Based on decision of the Supervisory Board who has established that one target (of two) MTIP 2008 have been achieved, in March 2011 was the payment for participants HT MTIP 2008. In accordance with targets achievements, payment of 50% of the total amount was made.

Currently are in progress HT MTIP 2009, HT MTIP 2010, Transitional HT MTIP 2011 and LTIP - Variable II 2011. All MTIPs have two targets which are equally weighted and cannot be changed during the MTIP duration. One target is based on the increase of the share price by a certain percentage; the second target is related to the share price movement compared to the complex return index.

The incentives themselves consist of 20 or 30% of the participants' individual annual salary as contracted on the beginning of the each MTIP, depending on the management level of the participant and according to the Supervisory Board decision. Participants' individual annual salary is defined as the annual amount of total fixed salary and the amount of variable salary in case of a 100 percent target achievement.

LTIP – Variable II has four equally weighted performance parameters and also cannot be changed during the LTIP durations. Two targets are financial KPIs, Earnings Per Share - EPS and adjusted operating Return On Capital Employed - ROCE, third target is customer satisfaction and fourth target is employee satisfaction.

The amounts awarded for LTIP – Variable II 2011 are for International Business Leaders (BLT's) – HT CEO is fixed sum specified in the individual employment contract, and for other participant is 30% or 20% of the participants' individual

annual salary as contracted on the beginning of the LTIP- Variable II 2011 depending on the management level of the participant and according to the Supervisory Board decision. Participants' individual annual salary is defined as the annual amount of total fixed salary and the amount of variable salary in case of a 100 percent target achievement.

In 2011 HT Matching Share Plan is introduced, following its implementation for DT Group International Business Leaders (BLTs). For the time being it is applicable only for the President of the Management Board (CEO), as a member of DT Group BLTs.

HT Matching Share Plan is established to ensure the long-term incentive effect and orientation towards the sustained development of the Company.

According to the provisions of the Plan, the participant is obliged to invest in HT shares, through a personal investment, minimum 10% and maximum 33,33% of his annual gross variable salary (Bonus/Variable I) paid for 2011.

These shares are to be held for a period of at least 4 years (lock-up period). After the lock-up period expires, one additional share (matching share) Company will grant for each share acquired as a part of the aforementioned personal investment.

Consequently, the new compensation model for the President of the Management Board (CEO) was introduced based on the above described Matching Share Plan.

1.4. Supervisory Board

Guido Kerkhoff

President of the Supervisory Board until 31 March 2011

Andreas Moelich

Member and president of the Supervisory Board from 4 May 2011

dr.sc. Ivica Mišetić

Deputy president

dr. Steffen Roehn

Member until 4 May 2011

Oliver Morbach

Member from 4 May 2011

Kathryn Walt Hall

Member

dr. Lutz Schade

Member

dr. Ralph Rentschler

Member

Andreas Hesse

Member

dr. Slavko Leban

Member

Juko Cikojević

Member

As specified by the Company, the chairman of the Supervisory Board receives remuneration in the amount of 1.5 of the average net salary of the employees of the Company paid in the preceding month. To the deputy chairman, the amount of 1.25 of the average net salary of the employees of the Company paid in the preceding month is paid while any other member receives the amount of one average net salary of the employees of the Company paid in the preceding month. To a member of the Supervisory Board who is in the same time the Chairman of the Audit Committee of the Supervisory Board in the amount of 1.5 of the average monthly net salary of the employees of the Company paid in the preceding month. To a member of the Supervisory Board who is in the same time a Member of the Audit Committee of the Supervisory Board in the amount of 1.25 of the average monthly net salary of the employees of the Company paid in the preceding month. To a member of the Supervisory Board who is in the same time a Member of the Compensation and Nomination Committee of the Supervisory Board in the amount of 1.25 of the average monthly net salary of the employees of the Company paid in the preceding month. DTAG representatives do not receive any remuneration for the membership in the Supervision due to a respective policy of DTAG. No loans were granted to the members of the Supervisory Board.

Compensation to the Supervisory Board members in 2011 is as follows:

	Period in which compensation is paid		Gross HRK
	From	To	
Juko Cikojević	1 February 2011	31 December 2011	144,044.38
Kathryn Hall	1 January 2011	31 December 2011	184,437.54
Slavko Leban	1 January 2011	31 December 2011	126,368.82
Ivica Mišetić	1 January 2011	31 December 2011	196,210.12
Josip PupiĆ	1 January 2011	31 January 2011	12,923.76

Since the remuneration of the Supervisory Board members is based on net average salary paid to the employees of the Company in previous month, only gross amounts are shown therein.

1.5. Corporate Governance Code Compliance Statement

Hrvatski Telekom d.d. (hereinafter referred to as “the Company”) has, in accordance with Article 250b, paragraphs 4 and 5 of the Companies Act (“Official Gazette” Nos. 111/93, 34/99, 121/99, 52/00, 118/03, 107/07, 146/08 and 137/09), prepared the Annual Report of the Management Board on the Status and Business Operations of the Company and the T-HT Group for the Business Year 2011 consisting of the Annual Report on the Status and Business Operations of the Company and the Consolidated Annual Report on the Status and Business Operations of the Company (hereinafter referred to as “Annual Report”), as well as the Corporate Governance Code Compliance Statement.

Given the fact that the Company’s shares are admitted to trading on a regulated market, the Company applies the Corporate Governance Code published on the web-site of the Zagreb Stock Exchange Inc. (www.zse.hr) and on the web-site of the Croatian Financial Services Supervisory Agency (www.hanfa.hr), and in effect as of 1 January 2011.

The Company complies with the recommendations of the Code, with the exception of those that were not, or are not practical for the Company to implement at the relevant time. These exceptions are as follows:

- The Company does not provide, without additional expense, proxies for shareholders who for whatever reason are not able to vote at the Assembly, such that those proxies will vote at the Assembly in compliance with the shareholders' instructions. Shareholders who are not in a position to vote in person at the Assembly by themselves should at their own discretion determine suitable proxies who are obliged to vote in compliance with the shareholders' instructions (Part 2.5.).

- At previous General Assembly meetings shareholders have not been given the opportunity to participate by means of modern communication technologies. Such participation will be implemented in the future to the extent that it is practical (Part 2.6.).
- The date on which the shareholder becomes entitled to payment of dividend was not set as recommended by the Code. The dividend date was set as the date of the holding of the General Assembly at which the decision on dividend payment was passed as in accordance with the Companies Act (Part 2.8.).
- The Supervisory Board is not composed mostly of independent members. Only two out of nine Supervisory Board members are independent members (Part 4.2.).
- Remuneration received by the members of the Supervisory Board is determined in relation to the average net salary of Company employees and not according to Supervisory Board members' contribution to the Company's business performance (Part 4.7.).
- The Compensation and Nomination Committee is not composed mostly of independent members of the Supervisory Board. One out of three Committee members is an independent member of the Supervisory Board (Part 4.12.1. and 4.12.2.).
- The Audit Committee is not composed mostly of independent members of the Supervisory Board. One out of three Committee members is an independent member of the Supervisory Board. Two remaining Committee members are external experts independent from the Supervisory Board (one of which is a financial expert, the other is an internal audit expert), both are employees of Deutsche Telekom (Part 4.12.3.).
- The Supervisory Board did not prepare an evaluation of its performance in the preceding period (Part 4.16.).
- The remuneration strategy adopted for Management Board and Supervisory Board members is based on Deutsche Telekom's Guidelines, adapted for local needs. The Statement on the policy of remuneration of the Management Board and the Supervisory Board was not composed separately. The remuneration of the Management Board and the Supervisory Board are disclosed within the Annual Report (Part 6.3.) performance (Part 4.7.).

Internal Control and Risk Management

The Audit Committee of the Supervisory Board of the Company was established in April 2002. The Audit Committee's principal responsibilities are the preparation of the decisions of the Supervisory Board of the Company and the supervision of the implementation of such decisions in relation to the controlling, reporting and audit activities within the Company. Revisions to the Audit Committee's term of reference were adopted in November 2006, amended in 2008 and adjusted in accordance with the Sarbanes Oxley Act and the Croatian Audit Act. The Audit Committee oversees the audit activities of the Company (internal and external), discusses specific issues brought to the attention of the Audit Committee by the auditors or the management team and makes recommendations to the Supervisory Board. The Audit Committee is responsible for ensuring the objectivity and credibility of the information and reports submitted to the Supervisory Board.

In executing its activities, the Audit Committee is authorized to:

- request the necessary information and supporting documentation from the management and senior employees of the Company and from external workers,
- participate at meetings held within the Company on issues that fall under the scope of activities and responsibilities of the Audit Committee,
- appoint advisors to the Audit Committee on a permanent basis or case by case if needed,
- obtain, at the Company's expense, external legal or other independent professional advice on any matter within its terms of reference provided that such advice is needed for the fulfilment of the Committee's scope of activities and responsibilities.

The Corporate Internal Audit of the Company performs an independent audit and control function on behalf of the Management Board and informs managers with comprehensive audit reports (findings and proposed improvements). Implementation of the annual Audit Program contributes to the minimization of risks and the improvement of operational efficiency. Audit Manual of the Corporate Internal Audit of the Company latest updated in December 2009.

The Financial Reporting Audit ensures the reliability of the Company's financial reporting by:

- Identifying risks and fields of improvement,

- Performing audits of areas of risk,
- Monitoring implementation of the audit measures and, if necessary, escalation of problems,
- Providing support in TOP projects in a way that would not conflict with the principles of objectivity and independence,
- Conducting ad hoc audits upon management request.

Significant Company Shareholders

On 31 December 2011, according to the list of the top ten shareholders of the Company published by the Central Depository & Clearing Company, significant Company shareholders are as follows. The majority owner of the Company is Deutsche Telekom AG, with 51 per cent of total outstanding shares. The Croatian War Veterans' Fund owns 7.0 per cent of shares, the Raiffeisen Mandatory Pension Fund holds 5.3 percent of shares and the Pensioner's Fund 3.5 per cent of shares. Remaining 33.2 per cent of shares are owned by Croatian citizens and by other domestic and foreign institutional investors. An up to date list of the top ten shareholders of the Company may be found on the Central Depository & Clearing Company web site.

The President of the Management Board of Hrvatski Telekom d.d., Mr. Ivica Mudrinić, owns 4,569 shares in total; Mr. Jürgen P. Czapan, MB Member until 31 March 2011, owns 185 shares in total; Mrs. Branka Skaramuča, MB Member, owns 200 shares in total; Mrs. Irena Jolić Šimović, MB Member, owns 45 shares in total; Mr. Ivica Mišetić, Ph.D., deputy Chairman of the Supervisory Board, owns 63 shares in total and Mr. Juko Cikojević, Supervisory Board Member (workers' representative, as of 1 January 2011), owns 263 shares in total.

Appointment of the Management Board, its functions and the Amendments to the Article of Association

The Members and President of the Management Board are appointed and removed by the Supervisory Board. Their term of office is up to five years, with the possibility of re-appointment. Pursuant to the Company's Articles of Association, the Management Board consists of between five and seven members. Currently the Management Board has six members: the President of the Management Board (CEO); MB Member and Chief Financial Officer (CFO); MB Member and Chief Operating Officer Residential (COO Residential); MB Member and Chief Operating Officer Business (COO Business); MB Member and Chief Technical and Chief Information Officer (CTO/CIO) and MB Member and Chief Human Resources Officer (CHRO).

The Company is offering fixed and mobile telephony services as well as wholesale, Internet, data and ICT services, organized into two business units, Business and Residential.

The Management Board needs prior approval from the Supervisory Board for the proposal of any amendments to the Articles of Association at the General Assembly.

Authorities of the Management Board Members

Pursuant to the Companies Act and the Company's Articles of Association, the Management Board has responsibility for managing the business affairs of the Company. It is obligated and authorized to perform all the activities and to pass all the resolutions that it considers necessary to successfully manage the business affairs of the Company, subject to such approvals as may be required from the Supervisory Board for certain matters and decisions.

Under the Articles of Association, the Company may be represented by any two members of the Management Board.

The Management Board was authorized by respective General Assembly decisions from 2009, 2010 and 2011 to acquire Company shares, with associated prior approval of the Supervisory Board to start the process of acquiring and managing of Company shares as in accordance with the authority given by the above mentioned General Assembly decisions. No Company shares were acquired during 2009, 2010 and 2011.

The composition and functions of the Supervisory Board

Pursuant to the Company's Articles of Association, the Supervisory Board consists of nine members. Eight members are elected by the General Assembly and one is appointed by the Company's employees. The Supervisory Board is responsible for the appointment and removal of Management Board members as well as for supervising the management of the Company's business affairs. Certain major or uncommon transactions such as large capital expenditure items, the assumption of long-term indebtedness or significant appointments require the approval of the Supervisory Board. The Supervisory Board established the Compensation and Nomination Committee and the Audit Committee.

2. BUSINESS REVIEW 2011

2.1. Croatian Telecommunication Market Overview

Strong performance despite negative economic trends

In 2011, T-HT Group successfully maintained its leading position in the Croatian telecommunications market across all services, despite further competitive pressure and falling consumption amid economic stagnation in Croatia.

Notable events in 2011 include the following:

- In February 2011, T-HT launched eBooking, a service that enables online booking of private accommodation.
- T-HT launched new mobile postpaid tariffs for consumers that include unlimited data usage.
- T-HT launched FlexBiz - new, simplified tariffs for SMEs and the "Internet for the team" data-bundling tariff for business customers.
- In May, T-HT launched five mobile Internet tariffs for consumer and business customers. Also in May, T-HT launched four new mobile postpaid group tariffs for consumers/families.
- T-HT launched new ICT services - tCloud and ICT LAN - for business customers.
- T-HT launched the Planet9 eBook store and "Spremalica," a multimedia content storage service for TV, mobile and PC/laptop.
- T-HT offered exclusive broadcasts of Croatia's Premier Football League to MAXtv IPTV users.
- In October 2011, T-HT launched MAX3 packages with a range of triple-play offers for consumers.
- In October 2011, T-HT launched a new Simpa offer for mobile prepaid users.
- T-HT's launched "MAXtv To Go" - making its IPTV services available anytime anywhere.

Market trends

Negative economic trends, new regulatory measures and growing competition significantly impacted the Croatian telecommunications market in 2011. In June, the Croatian telecommunications market saw further consolidation with the merger of VIPnet and B.net, which resulted in increasing competition in bundled telecommunications offers. In addition, regulation affecting Wholesale Line Rental (WLR) and naked bit-stream, which came into force in July 2011, means all operators are gaining full country-wide reach.

T-HT's revenues from voice services declined, on the back of decreased usage, reductions in the mobile termination rate and competitively priced offers from rival operators.

The key growth areas are broadband, data traffic and TV. During 2011, all major Croatian operators launched pay-TV and broadband offers, both mobile and fixed, in order to increase market share.

Mobile broadband is also experiencing significant growth, driven by continuously rising penetration of smartphones and other mobile broadband devices such as tablet computers. According to estimates by Nokia Siemens Networks, more than half a million smartphones and several hundred mobile applications for business, entertainment and information purposes were used in Croatia by the end of 2011. In the past year, the number of tablet computers increased from around 5,000 to almost 30,000. All three mobile operators in Croatia offer mobile TV services and around 1.4m Croatian citizens use social networks for communication, networking and sharing information/content.

The special 6% fee related to mobile services, introduced as an antirecession measure, remained in place throughout 2011.

Macroeconomic environment - No sign yet of economic recovery

Amid a lack of public sector reforms and investment to stimulate growth, the Croatian economy stagnated in 2011. According to the Croatian Central Bureau of Statistics, Croatian GDP showed modest growth of 0.7% in the first nine months of the year. Croatia's GDP growth for the whole of 2011 is expected to be around 0%. At the same time, further negative factors are emerging from the Eurozone: increasing cost of capital; declining demand for Croatian exports; and continued lack of investment. In 2011, unemployment rate in Croatia is still unfavorable, stood at 18.7% in 2011 (compared with 18.8% in December 2010). This unemployment rate has had a negative impact on personal consumption. Given the high levels of household debt (above the regional average) and stagnation of real income (0.3% lower in real terms for the first 10 months of 2011 against the same period of 2010), personal consumption growth has been minimal. Illiquidity rose again to HRK 40bn in October 2011. More than 76% of businesses have had their accounts blocked for longer than a year, and account for 83% of the total amount of overdue payments (or HRK 33.5bn).

Fixed-line market - T-HT maintained leadership in face of market decline

Fixed telephony remained highly competitive in Croatia with 10 active operators, including T-HT Group. VIPnet's acquisition of B.net is likely to increase the competition in bundled telecommunication offers.

T-HT successfully maintained its market leading position, however, with an estimated share of around 77%. This success reflects the Group's continuing dedication to high-quality services and improved marketing with offers tailored to suit the needs of specific customer segments. According to the Croatian Central Bureau of Statistics, the number of fixed-line minutes of use (MOU) decreased by 9% during the first nine months of 2011, following similar global trends. According to the Cullen International report for 2011, fixed-line penetration is estimated at 39% of the Croatian population at the end of 2011.

Mobile telecommunications - T-HT maintained dominant market position in shrinking market

T-HT, through its T-Mobile brand, remained the leader in a saturated mobile market, served by three operators since 2005. Mobile penetration rate was estimated to reach 120%¹ and the Company's share of total mobile customers was estimated at 47% at the end of 2011.

Mobile voice revenue declined in 2011 due to lower mobile termination rates and intense pricing competition. According to the Croatian Central Bureau of Statistics, total Croatian mobile market minutes of use (MOU) increased by 4.8%, but SMS traffic declined by 4.5% during the first nine months of 2011 compared with the same period of 2010 as users switched to social networks as a channel of communication. Demand for mobile Internet continued to grow in 2011, with all three mobile operators promoting their mobile broadband offers together with increasing smartphone and tablet computer offers. At the same time, hundreds of smartphone applications and new mobile services were introduced in 2011, such as e-books and mobile TV.

Internet - Fixed Broadband and Pay TV market continue to grow

T-HT's IPTV and DTH satellite TV services were enriched by new and exclusive sports content, and pay per view and "try and buy" offers. Satellite TV became an increasingly important element of the Group's TV offer.

At the end of 2011, the Group had 650,713 ADSL subscribers, compared with 629,228 users by the end of 2010. The number of IPTV customers at the end of 2011 was 340,743, representing 52.4% of T-HT's total ADSL customer base.

Despite the strong increase in broadband subscribers, the Croatian broadband market remains a significant growth opportunity for T-HT, with only 45% of Croatian households connected to fixed broadband compared to an average of more than 62% in Western Europe.

Data - Market migration to IP-based services continues

T-HT maintained its leading position in a market that is migrating from traditional unmanaged data services to more cost-effective, IP-based services. Although the data market is relatively small, representing less than 1% of total telecommunication market revenues, it represents an important service for business customers.

The Group's main data service competitors continued to develop their own networks, targeting the corporate and government sectors.

¹ From Q1 2011, the regulator (HAKOM) amended the definition of the total prepaid subscriber base so that only SIMs showing traffic or voucher recharges in the previous 90 days should be considered as subscribers: thus number of total mobile customers decreased and penetration rate is lower than reported in 2010.

Wholesale - New services introduced following new regulation

Liberalization of the fixed line market continued in 2011, with the introduction of Wholesale Line Rental (WLR) and naked bitstream services. WLR customers totalled 123,819 at the end of 2011.

As market liberalization continued in 2011, the number of Unbundled Local Loop (ULL) customers increased to 148,305 from 132,821 at the end of 2010.

In summary, during 2011, wholesale prices were amended for the following regulated services: bitstream access, call origination, call termination, cable ducts rental and unbundled local loop.

2.2. Regulatory Environment

Croatian Law on Electronic Communications, which replaced the previous Law on Telecommunications, has been in force since July 1st, 2008. This Law transposed the 2002 EU New Regulatory Framework onto Croatia's electronic communications market. Latest amendments to the Law on Electronic Communications were adopted by Croatian Parliament in July 2011 and entered into force in August 2011. Purpose of these amendments was to transpose the EU Regulatory Framework from 2009 onto Croatia's electronic communications market. Croatian operators were provided with a 90 days-period to consolidate their business operations with new provisions of the Law.

In line with Croatian regulatory framework, and taking into account the latest EU recommendations, the Agency can impose regulatory remedies only after analysing the market and determining the existence of significant market power (SMP). According to the market analysis conducted by the Agency in July 2009, and market analysis conducted in 2011, Company holds SMP position in the following markets:

1. call origination in fixed network
2. call termination in fixed network
3. wholesale (physical) network infrastructure access (including shared or fully unbundled access)
4. wholesale broadband access
5. call termination in mobile network
6. retail access to the public communications network at a fixed location
7. publicly available local and/or national telephone service provided at a fixed location for residential customers
8. publicly available local and/or national telephone service provided at a fixed location for non-residential customers

In these markets, remedies that were in place before the market analysis ceased to apply and the following remedies were imposed:

- in markets 1 - 5: network access and use of special network facilities (this obligation is extended to Company's optical fiber access network), non-discrimination, transparency, price control and cost accounting, accounting separation (applies only to Company's fixed business)
- in market 6: network access and use of special network facilities (obligation to offer wholesale line rental - WLR), non-discrimination, transparency, price control and cost accounting (notification of retail prices 30 days in advance; prohibition to unreasonably bundle services - introduction of naked DSL, provision of "pure" network access) accounting separation; in line with these obligations, Company published wholesale reference offers for naked bitstream and WLR in June /July 2011.
- in markets 7 and 8: Company and Iskon were imposed with price control obligations/promo-offers regulation.

In January 2011, the Agency imposed changes to Company's Reference Unbundling Offer (RUO) with almost 70 amendments, including the obligation to give access to the network even where there is no existing access line available,

introduction of VDSL technology, reduction in installation fees, and reduction of monthly fees for second and third access lines to the same end-user.

In March 2011, the Agency reduced Company's prices (monthly fees) charged for the wholesale unbundled local loop service (ULL) from HRK 52.14 to HRK 43.61. Company's monthly fee for Shared ULL was reduced in October 2011 from HRK 18.17 to HRK 16.92.

In May 2011, Agency issued a non binding interpretation of the decision dated 6 April, 2011 under which existing Carrier Pre-selection (CPS) customers shall be automatically migrated to WLR unless they make an objection within a reasonable period. In addition, on June 8th, 2011, Agency issued a decision imposing changes to Company's General Terms and Conditions for provision of services to its subscribers such that in the case of migration to WLR, a subscriber contract signed between the Company and its subscriber shall be automatically terminated (without the explicit request of the subscriber in question). Subsequently, on July 6th and 8th, 2011 Agency issued two decisions which amend Company's reference interconnection offer and reference offer for WLR in a way that existing CPS customers (customers who have contracted CPS before the reference offer for WLR came into force) may be automatically migrated to WLR without written request.

Decisions of this kind by Agency represent a significant intervention in the contractual relationship between the Company and its subscribers. As such, they are contrary to relevant regulations, including the general ordinance adopted by the Agency, and thereby discriminate against the Company in comparison to all other operators on which such obligations have not been imposed.

In addition, by these two decisions (dated July 6th and 8th) Agency has prohibited the Company to charge operators activation costs for wholesale services it provides them, thus forcing the Company to provide certain services to operators free of charge, i.e. at its own cost, as well as prohibiting Company from protecting its finances against debtors despite substantial undisputed debt on the part of the alternative operators to the Company. Such regulatory practice by Agency can be considered to have significant impact on Company's business and its related activities.

In October 2011, Agency determined that "three criteria test" for retail broadband Internet access was fulfilled, which qualified this market as susceptible to *ex ante* regulation. Finalization of market analysis and imposition of regulatory remedies is expected in Q1 2012. Proposed regulatory obligations relate to price control/promo offers regulation.

In addition, also in October 2011 Agency proposed to designate Company and Iskon as operators with SMP in the retail market for transmission of TV programs with remuneration, whereby rather strict regulatory remedies would apply both to Company's and Iskon's retail IPTV services. This procedure is pending, with expected finalization in Q1 of 2012.

Company is likely to be designated as SMP operator in remaining wholesale and retail (leased lines) markets, which are expected to be analyzed in 2012.

By its decision adopted in November 2011, Agency increased the "x" percentage that is used for calculation of Company's prices for wholesale *bitstream access* on copper - IP level (retail minus methodology), from 40% to 60%.

In December 2011, Agency adopted decision on amendments of Company's Reference offer for wholesale bitstream access on copper and FttH. This decision imposed more than 60 amendments and defined final concepts for the provision of wholesale bitstream access on copper and FttH.

In October 2010, the Company was (re)designated as the universal service provider for the next five years for all universal services (except for the subscribers' directory, which the Company can continue to provide on a commercial basis). Tariffs for universal services must be set at an "affordable level." Other tariffs, besides those mentioned above, are subject to ex-post review and are essentially unregulated.

Accounting separation (applies only to the Company's fixed business); cost accounting project, initiated at the end of 2008, is ongoing. In Q3 2011 the Agency started developing its own cost modelling for all regulated services.

The registration of pre-paid customers in mobile networks is underway.

2.3. Group strategy

T-HT Group Mission: Communication, Information & Entertainment, Always & Everywhere

Enormous volumes of photos and film clips are uploaded to the Internet and viewed every day, while virtual communities and social networks attract millions of new members every month. More and more, these applications are tailored to people's needs and can be used at any time through a wide variety of devices.

Checking e-mail and using the Internet are part of our everyday life. The Internet has revolutionized the way we spend our free time and the way we do business. We take for granted that we can access the Internet at home, in the office and on our mobile phones and we are constantly demanding faster access and better quality of service.

T-HT Group Vision: T-HT- Leader in Connected Life & Work

The possibilities are endless. Technology works for us, making life easier, solving problems faster, leaving us with more spare time and making our lives a lot more fun. We can do business on our way to the airport, watch our favorite TV show on the screen of a mobile phone and stay in touch with our families, friends and colleagues, using mobile and Internet-based services to share our experience, ideas, information and thoughts.

T-HT Group Strategy

The telecommunications market is undergoing a fundamental transformation, characterized by a dramatic increase in data traffic. By 2015, the average mobile customer will consume around 14 gigabits of data a month. In 2005, this figure was just a few megabits. Consequently, our strategy remains focused on building a robust broadband network, developing new services and providing ICT products and services alongside our core telecommunications offerings.

Our strategy remains based on three main pillars:

FIX - TRANSFORM - INNOVATE

FIX: strive to protect the Company's traditional fixed and mobile business.

TRANSFORM: continue the rollout of fast speed broadband networks to support expected rapid data growth and facilitate new services. At the same time, we are significantly transforming our cost structures to protect our business.

INNOVATE: focus on developing and expanding new growth areas by exploiting consumer and technology trends built around Internet, media and ICT services.

To achieve these targets, the Group has identified the following key strategic areas:

Connected Life and Work

Our strategic goal is the provision of innovative, converged services. The Group's strategic focus remains on broadband, both mobile and fixed, and broadband-related products such as IPTV, value-added services (VAS) and other content for growth, while exploring new growth segments.

Broadband and IPTV continue to offer the greatest opportunities for growth. Cloud computing and ICT also provide considerable growth potential. Furthermore, our networks, platforms and services enable us to support forthcoming changes in industries such as energy, healthcare and media.

Networks and Processes to facilitate the Gigabit Society.

Our infrastructure is key to the services we provide and we forecast a rapid increase in data volumes in the coming years. Our goal is therefore to continue to transform operations by improving efficiency and by supplying the bandwidth capacity

required. For this reason, we are focused on rolling out high speed fixed and mobile broadband networks and systematically implementing an all-IP proposition.

Cost Management and Efficiency Program

T-Hrvatski Telekom continuously maximizes the quality and efficiency of its operations by transforming and benchmarking its cost structure, while at the same time reviewing capital expenditure needs to support future growth opportunities. Together, these initiatives are intended to optimize Group operating costs and protect margins in an increasingly competitive environment.

Talent Management and Strategic Workforce Management

In a rapidly changing industry and with the strategic focus on new services and networks, T-Hrvatski Telekom continues to invest in new skills, talent management, education and training of staff. In this way, we are able to attract and retain first-rate people to help us build our business.

Regional expansion

The Group continues to monitor and evaluate expansion opportunities.

2.4. Organization of the Group

T-HT Group's operations comprise the Business and Residential units and centralized technical functions (CTO/CIO), support and steering functions (CEO, CFO and CHRO), along with a number of subsidiaries including Combis d.o.o., Iskon d.o.o. and KDS d.o.o.

Residential unit

Residential unit is headed by the Chief Operating Officer Residential (COO Residential) and in particular includes Marketing, Sales and Customer Service for residential customers.

Business unit

Business unit is headed by the Chief Operating Officer Business (COO Business) and in particular includes Marketing, Sales and Customer Service for business customers, ICT Business Solutions and Wholesale.

Organizational structure of the Group comprises:

- Management Board
- Customer Facing Units /Support and Steering Functions/ Technical Functions
- Sectors
- Departments
- Work Units

2.5. Residential Segment

Overview

- T-HT maintained its leading position in the mobile, fixed and IP market
- From Q1 2011, the regulator (HAKOM) amended the definition of the total prepaid subscriber base so that only SIMs showing traffic or voucher recharges in the previous 90 days should be considered as subscribers. Actual data for 2010 was adjusted in accordance with this
- New postpaid EXTRA tariffs were introduced with a particular focus on data
- The Simpa prepaid tariff was reintroduced
- The Group conducted continuous retention initiatives in both postpaid and prepaid segments
- T-HT successfully defended its fixed voice customer base
- The Group has 539,000 ADSL mainlines and 321,000 TV customers

- The Group is increasing coverage with a Direct to Home satellite TV service. Also offered exclusive TV content on MAXtv – Croatia’s Premier Football League, Formula 1 and launched MAXtv To Go – a TV service for smartphones, tablets, laptops and PCs.
- The Group launched MAX3 triple play offers

Major Achievements in 2011

HT a launched mobile acquisition and retention campaign for all new and existing customers signing 24-month contracts during first six weeks of the year. The strong focus on mobile broadband was further emphasized by the launch of new postpaid tariffs in March and new mobile Internet tariffs in May. Additionally, new Extra family tariffs were launched offering benefits for up to seven family members and including unlimited calls on the HT network. Extra tariffs also included a special offer targeting young people.

In October, the new rebranded Simpa tariff was re-launched, with attractive cross-network pricing, and a mobile number porting offer.

Bonbon, the prepaid brand aimed at young urban professionals, continued its growth with successful marketing campaigns where customers allow selecting convenient price points and members also receive promotional offers.

The new fixed tariff option ‘U mreži’ was also launched offering more attractive rates for calls to the T-Mobile network.

Fixed and mobile products were bundled in ADSL customer acquisition campaigns promoting bundled packages.

In TV, customer acquisition campaigns were offered in both IPTV and DTH satellite TV service. IPTV offers were focused on expanding sports content and the introduction of new pay-per-view services. Market leadership was reinforced through exclusive content such as MAXtv, Croatian Premier League football and Formula 1.

The MAX3 triple play was launched with specially designed packages combining voice, ADSL and IPTV services with attractive pricing. The launch of MAXtv To Go, a service for smartphones, tablets, laptops and PCs will make TV available everywhere and on all platforms.

The mobile subscriber base decreased by 1.9%, from 2,003,000 subscribers in 2010 to 1,964,000 subscribers in 2011, driven by a 3.6% decrease in prepaid subscribers, partly a result of migration to postpaid.

Minutes of usage per average subscriber in 2011 increased by 0.7% due to new, improved tariffs provided mainly in the prepaid segment.

Blended ARPU decreased by 11.0% in 2011, as a result of the economic situation and a highly competitive market.

By the end of 2011, total fixed access mainlines were 12.0% lower at 1,074,000. The decline was accelerated by the regulatory introduction of new wholesale products and was in line with the market trend of fixed to mobile and IP substitution. However, the Group maintained its competitiveness with attractive promotional offers and excellent service.

Fixed telephony users generated 2,083 million minutes in 2011. That was 10.2% lower than the previous year and reflects the impact of fixed substitution by mobile and IP traffic. Fixed voice ARPA decreased by 5.7%, as a result of general market trends outlined above.

By the end of 2011, the number of ADSL mainlines increased to 539,000, up 2.9%. At the same time, ADSL mainline ARPU fell 3.1%. The TV customer base showed strong growth. By the end of 2011, T-HT had 321,000 TV customers, an increase of 12.3%.

Satellite TV, an extension of the IPTV service, continues to grow after being repositioned and repriced in Q1 2011, offering more value for the customers.

2.6. Business Segment

Overview

- T-HT maintained leading position in the business segment in 2011
- Several ICT services were launched: tCloud Virtual Desktops, tCloud Human Resources, tCloud ERP, tCloud Virtual Private Servers and eBook store – Planet9
- Stable customer base across all segments
- New services Internet za tim and VPN private bill introduced to boost mobile customers
- Active customer retention efforts in both fixed and mobile
- My T-Business portal launched providing single location for managing all T-HT accounts
- HotHot – geo-marketing solution for business customers launched
- HT maintained leading position as major wholesale provider

Major Achievements in 2011

HT had 454,000 postpaid business subscribers by the end of 2011, marking a 4.4% increase in the customer base. Minutes of use (MOU) per average subscriber were down 5.0%, as a result of the economic downturn. That pushed blended ARPU down 8.9% compared with 2010. Mobile data grew in line with general mobile market trends.

At the beginning of 2011, HT launched a mobile acquisition and retention campaign for all new and existing customers signing 24 months contracts.

New Flex Biz tariffs, Mobile START and Mobile PLUS tariffs for SMEs were launched allowing customers to choose tariff package with a HRK 200 or HRK 600 monthly fee, allowing unlimited calls between two to eight team members.

The mobile data usage FlexBIZ option “Internet za Tim” was launched, introducing one traffic bundle to be used by the whole team.

In September, the VPN Private bill service was launched.

Other services available to T-Mobile customers include the revamped Applicentar product, as well as FormIt and Momentem.

HT also launched online book store Planet 9, service Spremalica providing free 10 GB bandwidth, and the HotHot geo-marketing application.

T-HT’s business fixed line customers declined 11.4% due to fixed to mobile and IP substitution, regulatory decisions, increased competition and economic recession.

Fixed telephony business users consumed 706 million minutes, down 17.5% on the previous year. As result of lower usage, ARPA decreased 10.0% to HRK 238.

The ADSL subscriber base is growing as a result of attractive and constant retention and acquisition campaigns, reaching 112,000 business users, an increase of 6.0%. ARPA decreased 2.5% to HRK 134.

The TV subscriber base has grown 12.4% to 19,000 customers as result of continuous improvements in services and programming. A range of promotional offers were available to both new and existing TV users.

The Hotel TV service was launched in March.

Offers around Christmas gave 50% off the monthly subscription fee for 12 months along with a free package of the subscriber’s choice (Sportski paket plus, HBO or Snimalica 10) for six months when signing up for 24 months.

The IP fixed line customer base increased 5.1%.

The VPN customer base increased 10.0%. T-HT constantly promotes the migration of existing traditional data customers to IP-based products.

The number of data lines fell 6.7% with traditional data lines decreasing, whilst Metro Ethernet service is growing.

Beside regular telecommunications services, T-HT built an ICT portfolio in 2011. At the start of the year, a Virtual Private Server service was launched and the Desktop Management product followed shortly after.

In July, Virtual Desktops – tCloud were launched and at the end of September, the first two modules of Software as a Service products were introduced – tCloud Human Resources and tCloud ERP.

T-portal

In 2011, tportal.hr continuously ranked among the top three web portals in Croatia according to reach, with more than 800,000 unique visitors per month according to Gemius, an independent internet traffic research agency.

The most important projects developed by tportal's editorial, creative and web-design team in 2011 include the following:

- <http://prvaliga.tportal.hr/>, a central information point regarding the national football league sponsored by Hrvatski Telekom. The site carries exclusive footage of goals and match highlights. It has attracted more than 100,000 unique visitors since its launch;
- <http://izbori2011.tportal.hr/>, a specialized portal for parliamentary elections in Croatia, with analysis, comment, in-depth event coverage as well as photo and video content;
- live streaming of several important events such as the T-Mobile INmusic festival, Zagreb Pride, election night highlights and a number of debates.

By the end of the year, tportal's Facebook page had acquired over 150,000 fans, which provided additional credibility to the portal's positioning in social networks.

In addition, tportal traditionally organizes the roman@tportal.hr award, a competition for the best Croatian novel.

Tportal's editorial, design and development team continued to improve the presentation of its services across a range of platforms. Content is available through mobile devices, SMS alerts and the T-Mobile WAP portal, along with social networks like Facebook and Twitter. In addition, T-Mobile iPhone users get a customized interface when browsing tportal.

Wholesale

Domestic wholesale market

During 2011, ULL market continued to grow with the gross additions of 15,500 new ULL lines. Operators were still highly focused on a fully unbundled local loop which provides a more attractive broadband services option, while the number of shared accesses is declining and is expected to disappear.

Based on the Agency decision, T-HT has updated and published its wholesale bitstream offer providing two additional products: naked bitstream on copper and FTTH bitstream. Nine operators signed contracts in 2011 for the wholesale bitstream service and eight have had started commercial operations by early 2012 (in accordance with the standard wholesale bitstream offer).

T-HT also published a new WLR (Wholesale Line Rental) offer. The new WLR product created a large amount of interest from CPS operators, resulting in rapid migration of existing CPS customers to the WLR service.

In 2011, four operators signed WLR contracts and there were 124,000 active WLRs. Subsequently, the number of pure CPS customers was reduced to a large extent. At the end of the year, 96,000 pure CPS active customers were reported.

A decrease in the number of customers generating origination traffic and the lower ARPU generated by these customers, meant that originated minutes fell by 9% in 2011. On the other hand, the number of terminated minutes into T-HT network remained stable.

The public consultation regarding the Wholesale Leased Line offer was finalised at the end of 2011. The Agency published its decision and specified changes required. The most important change is a new distance oriented pricing structure applicable for all technologies.

International wholesale market

Sales to international operators remained a significant part of total fixed wholesale revenue in 2011. The majority of international business is related to termination of international voice traffic into the Republic of Croatia and neighbouring countries. Incoming traffic to Croatia decreased by 14% and transit traffic to neighbouring countries declined 30%.

Despite of massive competition and price erosion in the international data and capacity market, due to the number of new contracts and interconnections and the growth in capacity sold, total business remained flat to the previous year. The IP business scored notable success with 125% growth of capacity sold to neighbouring countries, which boosted revenues.

On the cost side, the biggest success resulted from a strategic policy to force non-commercial international IP peering wherever possible, and reduce commercial IP upstream to appropriate levels. In 2011, T-HT's share of free of charge IP peering in total IP upstream rose to 52% from 13%. Reduced costs further enhanced the competitiveness of the T-HT offer in the IP market and, alongside intensified sales activities, were the main driver of revenue growth.

Intensive activity on the international network was key to strong business results. Continuous upgrades of capacity and technologies at international points of presence (Frankfurt, Vienna) and existing border crossings were carried out in 2011, and three new border crossings toward neighbouring countries were built, increasing the total number of border crossings to 32. A flexible and low-cost interconnection policy, enabled mostly through international points of presence, resulted in an increase in the number of international voice and data interconnections with global and regional operators: from 70 in 2010 to 92 in 2011.

During 2011, 31 new roaming partners were connected, increasing the total number to 391 roaming partners worldwide.

2.7. Network and Information Technologies

Network and Service Platforms

Network and Service Platforms are T-HT's core infrastructure, and are continuously upgraded and improved in line with the Group's strategy and marketing plans. Through the consolidation of its business operations, the Group started to converge the functionalities of its resources in both the fixed and mobile networks on joint service platforms, thus achieving improved availability of services and more cost efficient operations. In 2011, the Group further developed its network infrastructure, increasing broadband access capacity and establishing a common, fixed and mobile, transport and core network. In fixed networks, T-HT has adopted a strategy of providing all services mainly via one common broadband port. This has brought a transformation of its access network through the construction of a new optical access network, including an optical access platform (GPON) and selective modernization of the copper access network. Furthermore, the Group continued with functional upgrades of the existing PSTN network to enable VoIP telephony provision on broadband. In mobile networks, continuous radio access and core network transformation will support the development and rapid implementation of new, economically optimized technologies (e.g. HSPA, LTE), while facilitating maximum utilization of existing infrastructure and frequency resources. Mobile BroadBand (MBB) access was a key focus of development, through existing and newly deployed technologies such as UMTS900, in order to improve data services coverage. Expansion of the network by building new infrastructural points continued, along with capacity expansion to support a strong increase in data traffic.

Network infrastructure

Fiber optical infrastructure

The Group's activities were focused on deployment of FTTH (Fiber To The Home) on top of the existing FTTA (Fiber To The Area) infrastructure in order to increase RoI.

Electronic Communications Infrastructure Registration and Documentation

In order to fulfill regulatory obligations, a "Network Inventory Gateway" solution was implemented, enabling Web display of T-HT's linear ECI to the regulator (HAKOM).

Fixed access

DSL (Digital Subscriber Line)

The roll-out of DSLAMs (DSL Access Multiplexers) continued to provide broadband services for new customers.

Mobile access

Evolution and modernization of 2G and 3G radio access network

The total aggregation layer of the radio access network was modernized, as part of the evolution of the 2G network. The evolution of the 2G network, replacing existing 2G HW with next generation of multiradio equipment, is prerequisite for mobile broadband in rural areas and for the introduction of more energy efficient hardware and a smooth transition to LTE technology. A new revision of 3G SW has been installed to enhance the radio network, providing improved signaling schemes for smartphones and tablets, higher data capacity and allowing a greater number of concurrent users. Total data volume over the radio network increased by 119.6% from 2010. In June 2011, HSPA+ functionality was enabled in the 3G network. In the Bjelovar and Kutina regions, four test sites were equipped with UMTS900 technology, enabling wider coverage of 3G than standard UMTS2100. The technology utilized for national MBB coverage is UMTS900.

Rollout of radio network sites

The rollout of infrastructure is progressing in line with the revised implementation plan to enable the future development a proprietary network as well as renting out infrastructure to other operators.

Transport Layer

DWDM (Dense Wavelength Division Multiplex)

The division completed development of the DWDM-based transport network in the North-West area of Croatia to support connectivity of the redundant data centre in Varaždin with primary network sites in Zagreb. DWDM technology deployment enables fast provisioning of wholesale services fulfilling broadband capacity demand and brings opex savings.

Modernization of IP/MPLS network

Replacement of older generation P routers with new terabit routers at the Osijek and Rijeka site was completed.

Migration to IP

The migration of 3G sites from ATM (Asynchronous Transfer Mode) to IP (Internet Protocol) is completed, aiming to increase mobile broadband data speeds and to lower cost in order to higher access throughputs. The division also completed migration of the T-Mobile IP network to the T-Com IP public network.

Core Layer

Fixed core modernization

IMS core capacity was extended in accordance with PSTN migration plans. Migration from AXE based technology towards TSS/MGW (layered, IP based) technology continues.

Mobile core modernization

T-HT is the first operator within DT Group to embark on migration to R4 architecture (enabler for VoIP based services) and the migration of all traffic from R99 based network to the new R4 architecture was fully completed. The first phase of the project to introduce HD Voice on the 3G mobile network, based on WB-AMR codec, was successfully completed. To

support marketing requirements related to Mobile Internet (MI), a PCRF platform was successfully installed and integrated. PCRF platform has a central role in the network when detecting and applying different QoS ("Quality of Service") profiles depending on the category of user ("Quality Differentiation") and / or category of services (Internet, voice, video, mobile TV). The first phase of PCRF integration has enabled SSD ("Speed Step Down") functionality in the Mobile Internet service.

PSTN Migration

67,300 customers were migrated to VoIP (HALO service over a broadband access port). Preparations and installations have started for all-IP on 13 local exchange areas.

Service Layer

Service platforms for value added services

The remote device management HW and SW modernization project was completed. The existing system was upgraded with a firewall to enable selective blocking of SMS messages received from SMS centers outside RH per sender.

IP TV

PPV (Pay-Per-View) functionality was launched for special events on dedicated channels on the MAXtv platform. A web/mobile TV platform was installed and the MAXtv-to-go service was launched. Facebook services were launched on the MAXtv platform.

DTH

The MAXtv SAT platform was upgraded and end user devices were paired with high security software. T-HT installed and launched its own satellite uplink in the Varaždin Data center.

Portal services

In 2011, the new MyT Business self care portal with bill checking functionality was launched. The MAXtv portal was launched on tportal. Other new services included DLSI (Digital Life Store International), My phonebook and a new portal for SLA services. This portal is a reporting tool for external and internal customers and a proactive fault repair tool for internal users.

Service and Network Operations

For its internal telecommunications needs, HT began using VoIP services from its own portfolio, which makes it the largest business customer for all-IP telecoms services. All data communication between T-HT locations is IP based, and voice communications on the largest locations is VoIP. The automatic fault repair and quality of customer service tools were improved (automatic profile change) and a tool to monitor quality for IP-based voice services was developed and implemented.

Quality and Efficiency

The initial phase of a project to develop self-diagnosis and management of broadband services was completed. New tools for increasing efficiency were internally developed and implemented (including simpler CPE configuration, business services fault diagnostics, network migrations).

Provisioning and fault-repair

Proactive customer care

New tools for proactive customer support services were introduced and new channels of communication with the user were established. These enable the remote recognition of problems on customer sites so that customers can be contacted through a self-support portal.

Information Technology

Information Technology is one of the key business enablers in the telecommunications industry and a powerful tool for improving customer service. The Information and Business Systems Sector is responsible for information technology initiatives that support the Group's drive to increase revenues and improve internal efficiency, while enhancing product development and reducing time to market for new products. The division is particularly focused on improving service delivery processes and developing advanced customer, market and business intelligence capabilities. IT is recognized as the key enabler to bring process standardization and automation to a level where it can further improve internal efficiency and achieve optimal savings.

Notable achievements in the 2011 include:

- Billing system upgrade successfully completed, new functionalities introduced;
- Bill Formatter project initiated to standardize Invoicing process for both mobile and fixed services and support future business needs (e.g. convergent invoice, bundled packages). Phase 1 (invoicing for mobile services) completed;
- Billing components (mobile services billing system) - completed database upgrade as prerequisite for the new functionalities and migration to a virtual infrastructure;
- MPC (Multi Project Control) system for monitoring, ordering and controlling services from suppliers / sub-contractors and optimization and automation of internal processes further implemented to meet new business requirements;
- DCC (Data Center Consolidation) - completed consolidation of infrastructure for T-HT's data centers, business applications were migrated to the new infrastructure;
- OSS systems further developed to improve and optimize related processes and enhance services and equipment quality control and monitoring;
- Significant focus on the implementation of regulatory requirements - depersonalization of traffic data implemented for Geneva system, RUO updated, naked ADSL naked MAXtv, ELR implemented. Wholesale Rental Line, standard broadband offer updated; shared services monthly fees amended;
- Support for innovative ICT services based on 'cloud computing' principles - Virtual Private Servers Hosting and Virtual Desktop (tCloud Računalo) services rolled out. New services designed and implemented: ICT for SME - LAN services, ICT for SME - desktop services. SaaS solutions offered to the customers: Cloud Fleet management, tCloud Human resources, tCloud ERP, tCloud CRM.

Data and IT Security

The protection of data relating to customers, sales partners, employees, shareholders and telecom traffic is a key priority for T-HT. Mediation systems for fixed voice services and mobile services are certified according to the international ISO/IEC 27001:2005 standard. Systems security improvements resulted from Customer Data Security Assessment in conjunction with DTAG. New IT/NT security policies were approved and 31 Security Requirement based on these policies were approved. Preparations for PCI DSS certification moved into the final phase.

3. FINANCIAL REVIEW YEAR 2011

3.1. Group Financial Performance

Revenue

Throughout 2011, Group revenue was again impacted by the recession and special taxation measures that were adopted in response to it. Despite growth in the ICT business (classified as other service revenue), total revenue fell 3.6% to HRK 8,067 million (2010: HRK 8,372 million).

This revenue decline was primarily driven by lower voice revenue due to a highly competitive market, downward pricing pressure, a challenging economic environment and a tightening of the regulatory regime. The fall was offset to a degree by an increase in non-voice (data and broadband segment) and other service revenue (ICT segment).

Operating Expenses

Overall operating expenses fell 4.1%, or HRK 201 million, to HRK 4,749 million (2010: HRK 4,950 million), as a result of tight cost controls and lower costs related to lower usage and reduced interconnection fees.

Material expenses decreased by 6.4% to HRK 2,175 million, on a slight decline in Merchandise costs, down 0.9% to HRK 1,034 million, and a reduction in Services costs by 10.9% to HRK 1,141 million, mostly as a result of lower telecommunication services costs. At the same time, copyright fees rose as a result of growth in the Group's pay-TV subscriber base.

Total employee benefits increased by 8.2% to HRK 1,296 million as a result of higher redundancy provisions booked in 2011 (HRK 162 million vs HRK 31 million in 2010). Excluding redundancy costs, total employee costs fell by 2.9%, mainly due to a reduced number of employees resulting from the Group's ongoing program to rationalize business processes and drive efficiency improvements.

Other costs fell by 8.9% to HRK 1,292 million, primarily due to lower maintenance and advertising expenses.

The write-down of assets decreased significantly, by 41.4% to HRK 67 million, owing to better collection of unpaid bills supported by improved dunning procedures and legislation, while depreciation and amortization remained level with 2010 at HRK 1,414 million.

T-HT Group Profitability

While revenue fell 3.6%, EBITDA rose by 2.4% to HRK 3,782 million, before exceptional items of HRK 162 million, to give a 46.9% EBITDA margin (2010: HRK 3,694 million, 44.1%) on the back of a rise in other operating income and lower operating expenses. Operating profit (EBIT) fell 1.8% to HRK 2,205 million (2010: HRK 2,246 million), as a result of higher redundancy costs.

Net profit for 2011 was HRK 1,811 million, down 1.1% (2010: HRK 1,831 million), mainly as a result of higher redundancy expenses.

Balance Sheet

T-HT's balance sheet remains strong with total assets of HRK 13,136 million, down 2.9% (2010: HRK 13,529 million), mainly as a result of lower network investments.

Total non-current assets decreased to HRK 7,461 million at 31 December 2011 from HRK 8,008 million at 31 December 2010, due to lower investment in broadband access and core infrastructure.

An increase in total current assets to HRK 5,675 million at 31 December 2011 from HRK 5,521 million at 31 December 2010 was due largely to a stronger cash position as a result of a lower dividend payment compared with 2010.

Total issued capital and reserves decreased to HRK 11,019 million (2010: HRK 11,054 million), due to lower net profit in 2011. At 31 December 2011, cash and cash equivalents stood at HRK 3,704 million, compared with HRK 3,282 million at 31 December 2010.

Cash Flow

Cash flow from operating activities is T-HT's principal source of funds, enabling the Group to finance capital investments and dividend distributions. Cash flow from operations decreased by 8.5% to HRK 2,988 million (2010: HRK 3,266 million), mostly as a result of lower current liabilities driven by a reduced volume of purchases and lower capex realization.

Capital expenditure

Capital expenditure in 2011 (HRK 877 million) was down on 2010 by 23.9%, largely due to the slower realization of backbone and backhaul projects and the reprioritization of real-estate related projects.

The Residential segment saw slightly higher capital expenditure in 2011, primarily as a result of the change in treatment of Consumer Premises Equipment (CPE) from OPEX to CAPEX in the second half of 2010, and as a result of increased capital expenditure related to IT.

Business segment capital expenditure rose in 2011, due in large part to increased investments in business-related IT solutions as well as a change in the treatment of CPE equipment and increased investment in Group subsidiaries.

Capital expenditure in the Network and Support Functions segment was lower in 2011, mostly due to the slower realization of backbone and backhaul projects.

3.2. Analysis of segment results

Business units: Residential and Business

On 1 January 2010, the former divisions of T-Com and T-Mobile, serving the fixed and mobile markets respectively, were replaced by a new structure based on the Residential and Business segments. Starting from the first quarter of 2011, segmental reporting was introduced along these lines. In its financial reports, the Group's segments are reported by contribution to EBITDA level.

Residential Segment Financial review

Revenue

Total residential revenue in 2011 fell 4.4 % to HRK 4,433 million, largely on lower voice revenue both in mobile and fixed. This revenue trend has been driven by the slow economic recovery in Croatia, regulatory tightening and intensifying competition. Revenue was supported by one-off benefits, the revaluation of points related to a mobile loyalty program, the change of useful life of customer relationship and termination of a fixed loyalty program.

Voice revenue

Voice revenue at the end of 2011 was down 12.6% at HRK 2,582 million. Retail mobile voice revenue fell as a result of a highly competitive market, downward pressure on pricing and a harsh economic environment. In addition, voice mobile termination revenue was lower following reductions in termination rates. Mobile minutes of use (MOU) per average subscriber remained largely flat, so the revenue decline was the result of lower average revenue per usage (ARPU) arising from the tough economic environment. Fixed telephony revenue fell due to the continuation of fixed to mobile substitution, fixed to internet substitution, stronger competition and new regulation (such as WLR and naked ADSL regulation), leading to a 12.0% fall in the number of mainlines and a 10.2% decline in minutes of use. As a result of lower minutes spent and downward pricing pressure, voice average revenue per access (ARPA) declined by 5.7%.

Non voice revenue

Non voice revenue rose 6.1%, to HRK 1,500 million as a result of higher revenue from fixed services. Mobile services fell 7.2% to HRK 461 million mainly in prepaid segment, affected by economic crises and competitiveness that resulted with

price decreasing. In comparison with last year there is visible lower revenue from messages services that could not be compensated with data revenue growth. Fixed non voice (IP) revenue was boosted by a 2.9% increase in ADSL mainlines and a 12.3% rise in TV subscribers. ADSL ARPA fell 3.1%, mostly due to stronger marketing and promotional offers for ADSL access and usage.

Other service revenue

Other service revenue rose 189.7% to HRK 182 million as a result of higher revenue from usage bundle tariffs.

Terminal equipment

A decline of 19.3% to HRK 153 million in terminal equipment revenue was caused primarily by the prepaid segment, as investments in prepaid customers were reduced in 2011 through offering a more affordable range of handsets.

Contribution to EBITDA

In 2011, the Residential segment contribution to EBITDA totaled HRK 3,025 million, up 1.0%, primarily driven by 14.3% decrease in operating expenses. Lower operating expenses were largely the outcome of lower usage and non usage related direct costs. Lower usage related direct costs were the consequence of lower termination and roaming prices.

On the other hand, lower non usage related direct costs were caused by lower merchandise costs, as a result of different treatment of CPE equipment in the fixed business and lower investments in prepaid customers in mobile. Sales commission costs were also lower as a result of lower acquired and retained customers in the mobile business. Additionally, losses on accounts receivable were significantly reduced, as a direct benefit of better collection of unpaid bills, especially in the mobile segment. Copyright fees increased on the previous year, as a result of a 12.3% increase in payTV subscribers and expanded content offers such as MAXtv Premier League football and Formula 1. Indirect costs were lower than in 2010 as a result of savings initiated throughout the year to optimize and improve efficiency.

Business Segment Financial review

Revenue

In 2011, total business revenue fell 2.7 % to HRK 3,635 million. This fall was largely the result of lower voice revenue in mobile and in the fixed network.

Revenue in 2011 was supported by one-off benefits including the revaluation of points related to a mobile loyalty program, change of useful life of customer relationship and termination of a fixed loyalty program.

Voice revenue

Voice revenue fell 12.2%, to HRK 1,763 million. The fall was largely driven by a 10.0% decline in fixed retail voice revenue (HRK 75 million), largely driven by a fall in total minutes in traditional voice (-17.5%). This resulted in part from a decrease in total traditional voice mainlines (-11.4%) and from the migration to mobile voice. Fixed wholesale voice revenues fell 16.9% (HRK 61 million), due to NRA (Regulator) intervention in the form of lower interconnection prices from 1 January 2011. Voice services revenues from international operators fell by HRK 29 million, primarily as a result of lower traffic. Mobile voice revenues were 12.2%, or HRK 110 million, down at HRK 789 million, with retail accounting for a HRK 75 million fall and wholesale for a HRK 35 million decline. The HRK 48 million mobile voice revenue fall was mainly driven by lower voice ARPU (-8.9%) and lower average minutes per subscriber (-5.0%). A 4.4% increase in subscribers partially offset the revenue decline. Voice mobile termination revenue fell by 22.6%, or HRK 26 million, to HRK 90 million due to lower termination prices introduced by the NRA. A 17.2%, or HRK 35 million, fall in visitor voice revenue to HRK 170 million was driven by discounts as a result of new agreements with operators.

Non voice revenue

Non voice revenue fell 2.6%, to HRK 1,095. Fixed non voice revenue was 2.0% lower at HRK 787 million, as a result of a fall in retail revenue of 5.1%, which was partially offset by an increase in wholesale 3.8%. Fixed retail revenue decreased, on lower revenue from traditional data, which declined 17.8% owing to the migration to IP data, while the IP revenues remained flat. Non voice fixed wholesale revenue rose 3.8%, or HRK 11 million, to HRK 289 million. This was boosted by higher revenue from infrastructure, mostly because of WLR (Wholesale Line Rental) activations and international GIA (Global Internet Access). National leased lines revenue was lower, however, due to migration to new commercial models

and cancelation of capacities. Non voice mobile revenue fell 4.1%, or HRK 13 million, to HRK 308 million. Retail accounted for HRK 213 million of the totals, driven by mobile data, while visitor revenue declined by HRK 20 million, or 17.3%, to HRK 95 million as a result of new agreements with operators.

Other service revenue

Other service revenue rose 61.6%, or HRK 230 million, to HRK 606 million. This was primarily due to growth in the ICT segment following the acquisition of Combis (consolidated as of May 2010), and more proactive efforts to win ICT business.

Terminal equipment

Revenue from terminal equipment was down 6.6% to HRK 60 million, with fixed falling 57.9%, or of HRK 4 million, to HRK 3 million, while mobile was flat to the previous year.

Miscellaneous revenue

Miscellaneous revenue decreased by 31.5% or HRK 51 million, to HRK 110 million. The decline was driven in large part by mobile. In retail, disconnection fee revenue was reclassified as service revenue from the start of 2011, decreasing revenue by HRK 15 million. Mobile wholesale miscellaneous revenue decreased by 25.6%, or HRK 37 million, to HRK 107 million, due to lower national roaming (NR) prices and lower usage.

Contribution to EBITDA

The Business Segment contribution to EBITDA fell 5.8%, to HRK 2,287 million, driven largely by a HRK 99 million revenue decline. Operating expenses rose on higher merchandise costs, which were up 26.9% to total HRK 492 million, mainly due to merchandise costs from the Combis ICT business. Indirect costs were up 12.0%, or HRK 35 million, at HRK 327 million, due largely to the contribution of Combis. Interconnection costs in 2011 were down 18.9%, or HRK 107 million, at HRK 459 million.

Network and Support Functions Financial review

Contribution to EBITDA

Contribution to EBITDA rose by 11.6% to HRK -1,530 million. This is a result of higher other operating income by HRK 61 million and lower operating expenses by HRK 139 million.

Other operating income rose by 25.3% to HRK 301 million primarily driven by increase in revenue from charging of dunning letters and increase in revenue from provisions release.

Operating expenses fell by 7.0% to HRK 1,831 million from HRK 1,970 million. This drop was result of lower maintenance and advertising expenses.

4. CORPORATE RESPONSIBILITY

The T-HT Group strives to attain high standards of corporate responsibility across all its business segments.

Our ambition is to promote sustainable development, define best practice for high quality communications, promote the growth of an information and knowledge-based society and take the lead in highlighting the importance of environmental protection.

The T-HT Group believes that a company's reputation is dependent on far more than simply the quality, price or particular features of its products and services. Of equal importance are attitudes towards employees, customers, suppliers and investors, towards the environment and the society in which it operates. T-HT frames its corporate responsibility policies around positive interaction with all its stakeholders across all sections of society.

In this comprehensive Corporate Social Responsibility report, T-HT Group aims to outline and articulate its strong sense of responsibility towards its stakeholders, who range from customers, employees and suppliers, along with the broader society within which the Group operates.

Key CR strategy areas

Work/life balance

Our business is predicated on enabling the optimal work/life balance. Our goal is to develop innovative telecommunications solutions and services that will improve everyday life through first-class communications and connectivity.

An information and knowledge-based society

We aim to provide widespread access to telecommunications services to foster the growth of the knowledge society. Our ambition is to ensure that advanced technologies are available on-demand to all.

Creating a low carbon society

Environmental protection is a key goal of our social responsibility initiatives, and specifically involves responsible use of resources and a lowering of greenhouse gas emissions.

Principles of socially responsible conduct

T-HT Group bases its everyday operations on the following corporate values: ethical conduct; customer focus; mutual respect; team work; delivery of best results in the most efficient way possible; open dialog and responsibility to all stakeholders; and creation of an environment where efforts are recognized and results are valued.

Dialog with stakeholders

The T-HT Group firmly believes in the importance of open and transparent communication with all its stakeholders. The Group continued to engage with key audiences using the medium of social networks in 2011. T-HT communicates now with customers on a range of networks including Facebook, Twitter, YouTube and Flickr on a daily basis, to provide support in addressing problems and receive feedback on our products and service.

Transparent communication with investors is of particular importance in order to articulate the Group's current status and potential, to enable them to reach a fair valuation.

T-HT does not provide financial support to political parties or campaigns. For several years, however, the Group has been supporting initiatives aimed at combating corruption and its consequences, e.g. Transparency International.

Business compliance

The operations of the Group are based on integrity and compliance. This involves adherence to the law, following best practice and observing internal and external regulations. The Business Compliance Department, which was formed in 2008, promotes ethical business dealing across the Group and implements an Anti-Corruption Policy. The policy is designed to deal with issues related to conflicts of interest and corruption that may arise during the course of business.

Code of Conduct

T-HT's Code of Conduct sets clear standards of business conduct and is based on the highest ethical principles. The Code includes policies governing such issues as the giving and receiving of gifts and the Group now undertakes an annual planning exercise. This is based on an assessment of the risk of (non) compliance, using a methodology that can assist in the early detection of inappropriate business conduct and allow an appropriate reaction.

Certification

In 2007, T-HT joined the UN Global Compact initiative, which supports the fundamental social values within 10 principles of responsible business. In 2011, the T-HT Group reported, for the third time, on the implementation of these principles. In February 2011, T-HT joined the Croatian Business Council for Sustainable Development (HR PSOR), an organization that brings together representatives of the Croatian economy who share knowledge and innovative ideas to promote a balance between commercial success, social welfare and environmental protection. Oekom Research added T-HT to its Prime category, with respect to its standards of corporate responsibility and sustainable development policies, in 2008.

In 2011, T-HT was also included, for the third consecutive year, in the Vienna Stock Exchange's CEERIUS Sustainability Index for 2012. This rates shares in leading CEE region companies with respect to social and environmental, as well as economic, performance. Also in 2011, T-HT's Telecom Infrastructure Services Sector was awarded the Charter for Promotion and Implementation of Quality in the Croatian Economy by the Croatian Society for Quality.

Corporate responsibility

Our goal is to lead the way in corporate responsibility, and we are committed to sustainable and responsible activities at every point along the entire value chain. Our business activities are guided at all times by responsibility towards society, the environment, our employees, our customers and our suppliers

Responsibility towards society

The T-HT Group regularly cooperates with educational, cultural and scientific institutions, non-governmental organizations - especially those that focus on people with special needs and the disadvantaged, and organizations that promote the values of a civil society. Most projects are long-term initiatives, to ensure that they have a real impact. At the same time, employees of the Group also become personally involved in a number of projects. In this way, both the Group and its people participate directly in charitable works.

UNICEF

T-HT Group was UNICEF's first partner in Croatia, and we have built a strong relationship with the organization across the past seven years. In 2011, donations by T-HT supported the development of a new national model of early childhood intervention that, for the first time, puts the family at its centre. It also provides support to children with developmental issues. Alongside its corporate donation, T-HT has also provided a system whereby customers can also contribute to this valuable UNICEF project.

Another initiative the Group supported in 2011 was the Children's Rights Festival, which provided access to both sight and hearing impaired to enjoy a rich festival program including Croatian and international films.

"Zajedno smo jači" (Together We Are Stronger)

"Zajedno smo jači" (Together we are stronger) is an initiative that gives a key role to T-HT's employees in suggesting and selecting the charity projects to which the Company awards funds. In 2011, the sixth year of the initiative, 24 projects were chosen from 294 applications received from all over Croatia. T-HT donated a total of HRK 775,000 to these projects. Recipients of these donations included medical institutions and institutions working with the disabled, the elderly and with children.

060 lines - charity action support

In 2011, T-HT continued to support other charity campaigns by providing telephone lines to allow the public to make contributions, an activity it has engaged in since 2001. Campaigns and organizations assisted in this way in 2011 included the Ana Rukavina Foundation, "Društvo Naša djeca Vinkovci" (Our Children Association Vinkovci), Nada Vrbovec Association, the Autonomous Women's House Zagreb and "Dva skalina" (Two Steps Association). T-HT donated all proceeds from these initiatives to the causes concerned, raising a total of HRK 2.8 million for charity.

e-Etiquette for social networks

T-HT compiled the first Croatian handbook for appropriate behaviour on social networking sites, or e-Etiquette. The handbook defines formal and non-formal rules of conduct for Facebook, Twitter and other social networks. The Handbook has arisen from the rapid development of social networking in Croatia, which has outpaced the establishment of any framework for facilitating communication and understanding of the medium.

The handbook was compiled from submissions by everyday users of social networks and selected by an expert committee. The release of the e-Etiquette handbook coincided with three key anniversaries for T-HT in its communications history: 130 years of providing fixed telephony services; 20 years of mobile telephony; and five years of Internet TV.

Knowledge society

"Znanjem rastemo" (Growing through Knowledge) conference

In September 2011, T-HT held its fourth "Znanjem rastemo" (Growing through Knowledge) conference in Zagreb. The Group invites speakers to stimulate debate across society, academia and the business community and media, as well as its employees and customers. Guest speakers in 2011 were Nassim Nicholas Taleb, Ph.D., whose research focuses on issues such as happiness, risk, randomness, human error, probability and the philosophy of knowledge, and Amber Case – a cyber anthropologist who examines the way humans and technology interact and evolve together.

Support to expert conferences

T-HT also demonstrates its key role in developing the knowledge society through support it provides to gatherings of scientific experts such as WinDays 2011, the MIPRO Conference, the Combis Conference, the Cisco Conference, the Imagine Cup 2011 project, the Telecom Arena, the ICT Arena and other key thought leadership events related to the telecommunications sector and its communities. In addition, T-HT provided financial support, for the sixth consecutive year, to the Mediterranean Institute for Life Sciences.

The Group has also provided infrastructure, technical support and equipment to a number of local and international forums and conferences.

Cooperation with the academic community

T-HT's has a long-standing cooperation agreement with the Faculty of Electrical Engineering and Computing (FER), which originated in November 2006 with the Frame Contract on Cooperation in Scientific-Research and Development Activity, with a view to promoting transfer of knowledge and ideas between science and the economy.

T-HT also works closely with the Faculty of Law in Zagreb and it plans similar agreements with other faculties and universities, which in return offer a rich source of potential future recruits.

Scholarships

The Group announced the T-HT scholarship competition in 2011, an extension of a former T-Mobile project. Under the scheme, scholarships were awarded to six undergraduates, selected from the top candidates from the Faculty of Electrical Engineering and Computing in Zagreb, who have achieved excellent results at university, and also display a broad range of interests and participation in extracurricular activities.

Another scholarship is the "Korak u život" (Step into Life), organized by the Rotary Club Zagreb Kaptol, under which T-HT has awarded scholarships to five students who lack adequate parental support to fund further educational opportunities.

Culture

Museum of Contemporary Art

T-HT has been the primary partner of the Museum of Contemporary Art (MSU) since 2007. This partnership continued into 2011 with the annual award for the best Croatian contemporary work of art. T-HT provides telecommunications services to the museum alongside financial assistance.

T-HTnagrada@msu.hr

The fourth T-HTnagrada@msu.hr, one the most prestigious annual awards in the field of contemporary art in Croatia, was held in 2011, and a record number of art works were submitted. An international jury selected the winning submissions which, this year, were purchased and included in T-HT's collection, on show in the new building of the Museum of Contemporary Art.

Theatre

T-HT continued its tradition of sponsoring Croatian national theaters in Osijek, Split, Rijeka and Varaždin and the Gavella City Drama Theater in Zagreb. The "Špancirfest" street festival and Varaždin Baroque Evenings were supported through sponsorship of the City of Varaždin.

Film festivals

In 2011, T-HT supported a number of film festivals: the Pula Film Festival, the Vukovar Film Festival, Zagrebdox, the Zagreb Film Festival, Film Mania and the Forum Film Zadar.

The roman@tportal.hr prize

Tportal ran its fourth competition for the roman@tportal.hr literary prize worth HRK 100,000.

T-Mobile INmusic festival

In 2011, T-Mobile supported the INmusic Festival for the third time. This is Croatia's largest open-air festival and it showcased more than 40 international and local performers on six stages. British daily newspaper The Times rated T-Mobile's INmusic Festival among the top 20 festivals in Europe.

Electronic Beats Festival

T-HT supported the first ever Electronic Beats Zagreb Festival, which attracted 1,500 visitors who enjoyed performances by some of the hottest performers on the current electronic music scene.

Sport

Croatian Olympic Committee

The T-HT Group continued its long-standing cooperation with the Croatian Olympic Committee, as its main sponsor, thus linking T-HT's values with the Olympic Games principles of fair competition, persistence and the pursuit of excellence.

MAXtv Premier League

In 2011, MAXtv launched exclusive broadcasts of Croatia's Premier Football League matches. The cooperation between MAXtv and the Croatian Premier Football League brings premium production quality and shows top-flight Croatian football matches on new interactive platforms. T-HT also sponsors the Croatian Premier Football League.

Sportske igre mladih (Youth Sports Games)

T-HT is a long-standing sponsor of the Youth Sports Games, the largest amateur sports event in Croatia. In 2011, more than 80,000 competitors from 7 to 18 years old came together to compete in 10 sports. The event is underpinned by a strong anti-drugs, anti-alcohol and anti-violence message.

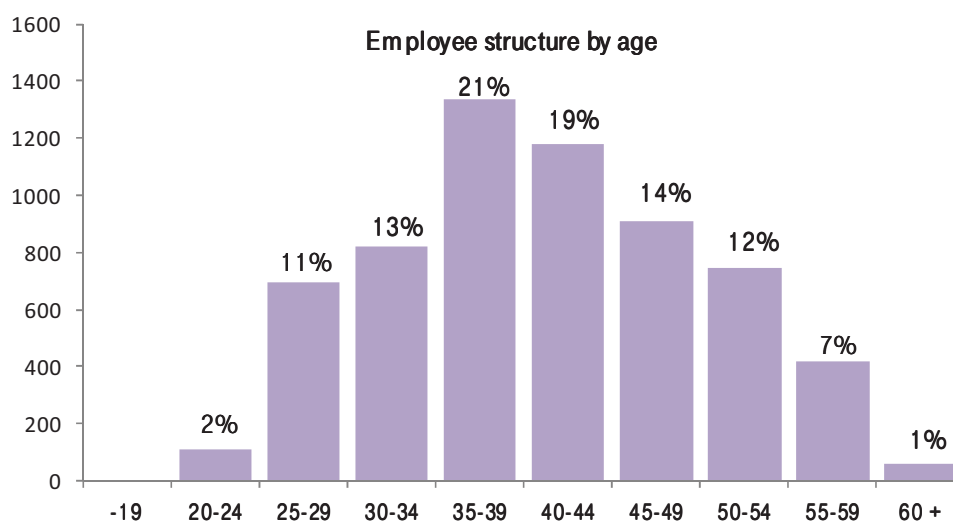
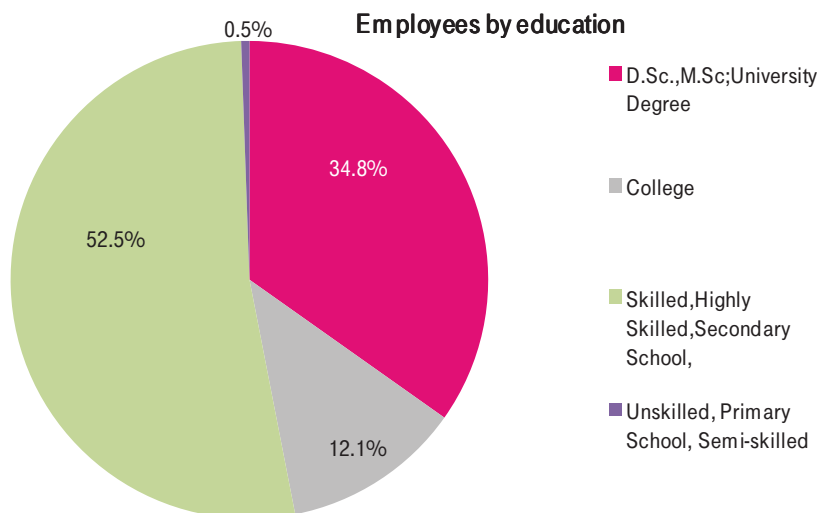
Responsibility to employees

Against a backdrop of economic crisis, the key challenge facing T-HT has been maintaining investment in employee development, to ensure a workforce that is motivated to provide quality customer service and maintain the competitiveness of Group.

To address this challenge, the Group focused on achieving greater levels of knowledge and resource sharing to maximize its restricted resources and encourage employee development. At the end of 2011, the Group had 6,032 employees (full-time equivalent).

Career development

The Group introduced a career development plan for managers (StepUP!) in 2006. This has now been reinforced by career development program for all employees (GoAhead), introduced in 2011. Under this plan, the most promising employees are offered additional opportunities for career development such as transfer to another business area, international experience, or other career development initiatives.



Management career development

In 2011, the management development initiative was based around mutual sharing of knowledge and experience. Programs were created with the aim of increasing manager competencies by learning from colleagues. Managers participated in the “Closer to the Customer” program, which included training at points of sale, call centers or field visits with technicians. They were also provided with opportunities to improve management skills through experience sharing sessions, facilitated by a professional coach.

Project management career development

With the need for high quality project management paramount, T-HT introduced a career structure for project managers, giving access to wider range of career development opportunities. Employees who opted for this career path have been given clearly defined progress and development criteria, as well as opportunities for acquiring highly regarded project management qualifications.

Knowledge on Thursdays

The Group continued its “Knowledge on Thursdays” lectures throughout 2011. Experts from varying parts of the business shared knowledge and experience with colleagues on topics including the network, new technologies, products and services, energy consumption, customer satisfaction, legal issues, data protection and security and business compliance.

Additional employee benefits

HT provides a range of benefits aimed at promoting health and wellbeing, including a free annual medical check-up and the opportunity to participate in a range of cultural and sports activities funded by the Company. The Company also offers incentives to join the HT pension scheme.

HT's respect for diversity and equal opportunities is clearly exemplified by the proportion of women holding senior management roles within the Company, which is above the national average.

Responsibility towards the customers

Customer care

Customer care and satisfaction are the key focus of HT's Call Center activities. Its agents are ready to answer all questions or provide support on a 24/7 basis, by phone, e-mail, postal mail and fax. The Call Centre plays a key role in the maintenance of good relations with customers. Besides providing information, it also sells products and services tailored to customers' individual needs.

Monitoring customer satisfaction

T-HT continuously monitors customer satisfaction and loyalty, using the TRI*M methodology. This enables T-HT to evaluate the efficiency of business processes within the Group and identify where improvement is required.

Responsible approach to customers

T-HT tailors its services to take into account the varying needs of its customers' needs, as evidenced by special discounts, shops accessible to disabled people, special packages for customers on low incomes, services for young people, discounts granted to Croatian Homeland War disabled veterans, the MAXtv parental protection, protection for Internet users and various billing options such as web billing, voice billing and e-billing. In addition, T-HT complies with the Code of Advertising Standards, which prescribes advertising rules and principles.

Advanced technology available to all

As leader and innovator in the Croatian telecommunications market, T-HT continues to invest in the development of innovative technologies, broadband, IPTV and LTE technology. T-HT was the first operator in Croatia to offer the opportunity to test the most advanced LTE network, which provided up to 10 times higher data transmission rates.

tCloud

In 2011, the Group also started offering new and innovative services in the cloud. The tCloud Računalo (tCloud Computing) service enables business customers to use a virtual IT infrastructure without the cost of IT equipment – and it also saves energy. For residential customers, Spremalica (Data Storage) and Sinkronizacija podataka (Data Synchronization) services, provide easy and secure online storage and content sharing capabilities.

Planet9

T-HT's Planet9 online bookshop and Planet9 e-book reader enables access to a virtual library at any time and any place.

MaxTV To Go

T-HT's Internet TV offering has been expanded with a new service called MAXtv To Go. This enables viewers to watch MAXtv on the move, via mobile handsets and computers, and on additional screens at home.

HotHot

HotHot, the first local geo-location application in the Croatian language, gives smartphone owners an easy and practical overview of attractive consumer offers in the vicinity.

Responsibility towards the suppliers

T-HT implements a Sustainable Procurement Program for the purchase of products and services within the entire Group. The Group endeavours to obtain optimal value whilst considering factors such as price, quality, availability and

functionality, the impact of product and/or service on the environment, social aspects, working conditions and human rights.

The Sustainable Procurement Program includes supply chain management with regard to social and ecological risks and the possibility of long-term benefit for the Company, supplier selection under clearly defined minimum standards (including Social Charter or International Labour Organization conventions), and regular checks to ensure compliance.

Responsibility towards the environment

Afforestation of fire affected areas

T-HT continued with its project of afforestation of areas affected by fire for the fourth consecutive year, with direct investments into extensive, ecologically important areas. In 2011, the project planted 27 hectares of burned forest area with seedlings of Aleppo pine, cypress and pine trees. T-HT employees also joined the project as volunteers 2011.

Promoting ecological awareness in T-HT

T-HT has striven to encourage a strong understanding of environmental issues amongst its staff. To this end, 2,000 employees undertook an online course about environmental protection and more than 250 employees, whose daily work duties can significantly impact the environment, attended lectures about environmental protection.

T-HT's car fleet totals around 220 LPG operated vehicles. LPG is considered the most environmentally friendly motor fuel. To encourage employees to use LPG, T-HT has devised a system for awarding the most environmentally aware drivers.

Ecological disposal of used mobile devices

Since 2005, when organized collection and recycling of used mobile phones started, T-HT has assisted in the disposal of more than 111,000 mobile phones. Alongside the regular collection of used devices in T-Centers, the focus in 2011 was on raising public awareness about the importance of this activity. A successful ecological and education project aimed at collecting old mobile devices was completed in cooperation with the elementary school "Jure Kaštelan" in Zagreb.

T-HT also partnered a project for collecting used mobile devices called "S manje gnjavaže do reciklaže" (Hassle-Free Recycling), undertaken by students of the Faculty of Economics and Business.

Implementation of green technologies

As the only telecommunications company certified under the ISO 14001 Environmental Management Standards, T-HT focused on the implementation of green technologies in telecommunications. The Group is witnessing major technological changes, and the aim is to align these changes with high ecological standards and in this way contribute to the quality of life and business of our customers and wider community.

Energy efficiency

The mobile, fixed and Internet networks present an immense challenge in terms of electric power consumption and energy efficiency. Every new service, subscriber increase and network development leads to greater energy requirements. T-HT launched a project to promote energy efficiency at corporate level. The main initiatives here include efficient air conditioning and power supply systems, modernization of telecommunications equipment, optimization of the real estate portfolio and renewal of property owned by T-HT according to energy efficiency principles, more extensive use of IT resources along with a range of other activities that can contribute to more economical consumption of energy.

Role of ICT in environmental protection

Given the increasingly important role that technology plays in environmental protection, in 2011 T-HT representatives participated in a workshop on sustainable development and green ICT within a MIPRO conference. T-HT also provided keynote speakers at the 68th International Session of the European Youth Parliament, addressing the topic of climate change before the Committee on Industry, Research and Energy. The Group also participated in the largest global initiative against climate change called - the "Earth Hour".

Certification and membership

T-HT has held the ISO 14001 certificate for environmental protection since 2010. In June 2011, the ISO 14001 audit was successfully completed, which confirmed the integration of environmental protection in all processes and the work of all

employees according to the prescribed level, and that all employees are aware of the importance of environmental protection.

T-HT is also a member of the European Telecommunications Network Operators' Association (ETNO) and a signatory to the Environmental Protection Charter and Sustainable Development Charter.

Corporate responsibility within affiliated companies

Combis

At Combis, the key focus is on the promotion of excellence and social development. In 2011, Combis supported, through donations and sponsorships, a range of projects in the arenas of education, sport, health and culture. In 2011, Combis financially supported young information scientists from V. High School in Zagreb and made it possible for them to participate in the final round of the International IT Competition in the USA. Combis also recognized the work and innovation in sustainable development conducted at the Faculty of Engineering, University of Rijeka, by a team of young engineers who are working on the design and production of electric car and plug-in stations.

As part of its efforts to promote education Combis also supported the "Priatelji talenata" (Talents' Friends) fund which provides financial support to talented and needy students. Combis also promotes sport and health. In 2011, it supported athletes both young and old. For the young sporting stars of the future, Combis assisted with the purchase of jerseys for participants in the Youth Academy of Trnje Football Club, which brings together more than 200 children. More established athletes benefited from Combis' support for the top event of the athletic season in Croatia – the IAAF World Challenge Zagreb, also known as the Boris Hanžeković Athletic Meeting. In the realm of urban culture, Combis supported "Crtani Romani Šou" (Comics Show) association and became the exclusive ICT partner of the 14th International Comics Festival, which took place in November in Zagreb. Combis also supports those most in need, working alongside the Croatian Rotary Association and a project of providing assistance to mine victims to provide first aid and medical care, physical rehabilitation, psychological support and social reintegration, as well as professional and economic rehabilitation. Combis traditionally supports industry events, and its sponsorship activities included Cisco Expo partner conferences, Microsoft WinDays conference, IBM Forum, Oracle - The Information Age in Zagreb, Sarajevo and Beograd, ICTI – International Conference of the Information and Communication Technology and Security and IDC Cloud Computing Roadshow conference in Budapest. For the fifth time, in 2011 Combis organized the Combis conference in Opatija, which gathered more than 300 participants from Croatia and the region, from the area of finance and telecommunications, state administration, and industry. Under the umbrella topic 'Competence. Excellence', the top ICT experts gave lectures, presentations, and case studies, sharing knowledge and experience and thus contributing to the development of competence and business excellence.

Iskon

Throughout 2011, Iskon supported a number of social and cultural projects. Iskon was the sponsor of telecommunications services at the Motovun Film Festival and also sponsored the Best Short Film award - "Motovunski kratki" - for the third consecutive year. Iskon also made available to users of Iskon.TV all films that were shortlisted for the award on the eve of the Festival. Iskon has been partner of the Croatian National Football Team and sponsor of the "Uvijek vjerni" (Always Faithful) fan club for ten years. With the signing of a new contract with the Croatian Football Federation in 2011, the cooperation was extended for another two years. In the upcoming period, Iskon will continue to be the official internet provider of the Croatian Football Federation and provide hosting and maintenance of the Croatian Football Federation web pages, as well as hosting of the web page of the "Uvijek vjerni" (Always Faithful) fan club. In 2011, Iskon also extended its cooperation with the table tennis club HASTK Mladost Iskon. In 2011, Iskon was the official sponsor of telecommunications services at the ATP Zagreb Indoors and Zagreb Open tennis tournaments, for the third consecutive year. In 2011, the first augmented reality exhibition was held in Croatia, organized by Zagreb Art Kolektiv (ZARK), under the sponsorship of Iskon. In augmented reality certain models, photographs or video content are placed within the physical world using QR code, and then observed via mobile handset screens. The works of art were displayed on several locations in Zagreb. In 2011, Iskon also supported the CARNet annual conference CUC (CARNet Users Conference), the international convention on information and communications technology, electronics and microelectronics MIPRO and KOM, a conference on electronic communications technologies and standards in IT.

5. APPENDIX

5.1. Financial Statements

Consolidated income statement

in HRK million (IFRS HT accounting policies)	Jan-Dec 2011	Jan-Dec 2010	% of change A11/A10
Voice revenue	4,345	4,963	-12.5%
Non voice revenue	2,595	2,539	2.2%
Other service revenue	788	439	79.5%
Terminal equipment	213	253	-16.1%
Miscellaneous	126	177	-28.8%
Revenue	8,067	8,372	-3.6%
Other operating income	301	240	25.3%
Total operating revenue	8,369	8,612	-2.8%
Operating expenses	4,749	4,950	-4.1%
Material expenses	2,175	2,325	-6.4%
Employee benefits expenses	1,296	1,198	8.2%
Other expenses	1,292	1,419	-8.9%
Work performed by the Group and capitalised	-81	-105	23.0%
Write down of assets	67	114	-41.4%
EBITDA	3,619	3,662	-1.2%
Depreciation and amortization	1,414	1,415	-0.1%
EBIT	2,205	2,246	-1.8%
Financial income	83	71	15.9%
Income/loss from investment in joint ventures	15	11	40.4%
Income from investment in associates	0	2	-100.0%
Financial expenses	48	55	-13.0%
Profit before taxes	2,255	2,275	-0.9%
Taxation	444	444	-0.1%
Net profit	1,811	1,831	-1.1%
Minority interest	0	0	-809.2%
Net profit after minority interest	1,811	1,831	-1.1%
Exceptional items	162	32	412.0%
EBITDA before exceptional items	3,782	3,694	2.4%

Consolidated balance sheet

in HRK million (IFRS HT accounting policies)	At 31 Dec 2011	At 31 Dec 2010	% of change A11/A10
Intangible assets	999	1,162	-14.0%
Property, plant and equipment	5,953	6,336	-6.0%
Non-current financial assets	435	422	3.1%
Receivables	23	24	-5.3%
Deferred tax asset	52	64	-18.9%
Total non-current assets	7,461	8,008	-6.8%
Inventories	175	216	-19.0%
Receivables	1,307	1,448	-9.8%
Current financial assets	363	465	-21.9%
Cash and cash equivalents	3,704	3,282	12.9%
Prepayments and accrued income	126	110	14.9%
Total current assets	5,675	5,521	2.8%
TOTAL ASSETS	13,136	13,529	-2.9%
Subscribed share capital	8,189	8,189	0.0%
Reserves	409	409	0.0%
Revaluation reserves	-3	-1	-235.8%
Retained earnings	612	626	-2.2%
Net profit for the period	1,811	1,831	-1.1%
Minority interest	1	0	2090.1%
Total issued capital and reserves	11,019	11,054	-0.3%
Provisions	271	293	-7.6%
Non-current liabilities	32	43	-24.9%
Total non-current liabilities	303	336	-9.9%
Current liabilities	1,492	1,682	-11.3%
Accrued expenses and deferred income	153	324	-52.9%
Provisions for redundancy	169	133	27.4%
Total current liabilities	1,814	2,139	-15.2%
Total liabilities	2,117	2,475	-14.5%
TOTAL EQUITY AND LIABILITIES	13,136	13,529	-2.9%

Consolidated cash flow statement

in HRK million (IFRS HT accounting policies)	Jan-Dec 2011	Jan-Dec 2010	% of change A11/A10
Profit before tax	2,255	2,275	-0.9%
Depreciation and amortization	1,414	1,415	-0.1%
Increase of current liabilities	0	73	-100.0%
Decrease of current receivables	65	0	-
Decrease of inventories	41	40	3.7%
Total increase of cash flow from operating activities	3,776	3,804	-0.7%
Decrease of current liabilities	-375	0	-
Increase of current receivables	0	-48	100.0%
Other cash flow decreases	-413	-489	15.6%
Total decrease of cash flow from operating activities	-788	-537	-46.6%
Net cash inflow/outflow from operating activities	2,988	3,266	-8.5%
Proceeds from sale of non-current assets	3	13	-73.8%
Proceeds from sale of non-current financial assets	74	473	-84.4%
Interest received	57	31	84.1%
Dividend received	0	6	-100.0%
Other cash inflows from investing activities	990	224	341.6%
Total increase of cash flow from investing activities	1,125	747	50.5%
Purchase of non-current assets	-877	-1,153	23.9%
Purchase of non-current financial assets	0	-290	100.0%
Other cash outflows from investing activities	-944	-694	-36.1%
Total decrease of cash flow from investing activities	-1,821	-2,136	14.7%
Net cash inflow/outflow from investing activities	-696	-1,389	49.8%
Total increase of cash flow from financing activities	0	0	-
Repayment of loans and bonds	-11	-4	-165.2%
Dividends paid	-1,863	-2,788	33.2%
Total decrease in cash flow from financing activities	-1,874	-2,792	32.9%
Net cash inflow/outflow from financing activities	-1,874	-2,792	32.9%
Exchange gains on cash and cash equivalents	4	2	100.0%
Total increase of cash flow	2,992	3,269	-8.5%
Total decrease of cash flow	-2,570	-4,181	38.5%
Cash and cash equivalents at the beginning of period	3,282	4,195	-21.8%
Net cash (outflow) / inflow	422	-912	146.2%
Cash and cash equivalents at the end of period	3,704	3,282	12.9%

Residential Segment

in HRK million	Jan-Dec 2011	Jan-Dec 2010	% of change A11/A10
Voice revenue	2,582	2,955	-12.6%
Non voice revenue	1,500	1,414	6.1%
Other service revenue	182	63	189.7%
Terminal equipment	153	189	-19.3%
Miscellaneous	16	17	-2.9%
Total revenues	4,433	4,638	-4.4%
Operating expenses	1,407	1,642	-14.3%
Contribution to EBITDA before SI	3,025	2,996	1.0%

Business Segment

in HRK million	Jan-Dec 2011	Jan-Dec 2010	% of change A11/A10
Voice revenue	1,763	2,008	-12.2%
Non voice revenue	1,095	1,125	-2.6%
Other service revenue	606	376	61.1%
Terminal equipment	60	64	-6.6%
Miscellaneous	110	161	-31.5%
Total revenues	3,635	3,734	-2.7%
Operating expenses	1,348	1,306	3.2%
Contribution to EBITDA before SI	2,287	2,428	-5.8%

Network & Support Functions Segment

in HRK million	Jan-Dec 2011	Jan-Dec 2010	% of change A11/A10
Other Operating income	301	240	25.3%
Operating expenses	1,831	1,970	-7.0%
Contribution to EBITDA before SI	-1,530	-1,730	11.6%

Capex by Segment

in HRK million	Jan-Dec 2011	Jan-Dec 2010	% of change A11/A10
Business	86	69	24.3%
Residential	330	258	27.7%
Network and Support Functions	461	825	-44.1%
T-HT Group	877	1,153	-23.9%

Statement of the Management Board of Hrvatski Telekom d.d

To the best of our knowledge, financial statements of the company Hrvatski Telekom d.d. (hereinafter: "Company") and audited consolidated financial statements of the Company and affiliated companies thereof (hereinafter: "Group"), which are prepared in accordance with International Financial Reporting Standards (IFRS), give a true and fair view of assets and obligations, profit and loss, financial position, and operations of both the Company and the Group.

The management report for the year 2011 together with other documents made public contain a true presentation of development and results of operations and position of the Group, with description of significant risks and uncertainties for the Group as a whole.

Mr. Ivica Mudrinić, President of the Management Board (CEO)

Mr. Dino Ivan Dogan, Ph.D., Member of the Management Board and Chief Financial Officer

Mr. Johan Busé, Member of the Management Board and Chief Operating Officer Residential

Ms. Irena Jolić Šimović, Member of the Management Board and Chief Operating Officer Business

Mr. Božidar Poldrugač, Member of the Management Board and Chief Technical Officer and Chief Information Officer

Ms. Branka Skaramuča, Member of the Management Board and Chief Human Resources Officer