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July 24, 2020



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Krapinska 45  
10000 Zagreb

SECURITY: ERNT (ISIN: HRERNTRA0000)  
LEI: 5299001W91BFWSUOVD63  
HOME MEMBER STATE: Republic of Croatia  
REGULATED MARKET SEGMENT: Regular Market of the Zagreb Stock Exchange

# Ericsson Nikola Tesla d.d.

Management Report on the Company and Ericsson Nikola Tesla Group business performance with comments on the financial results for H1 2020

### Highlights:

- Sales revenue: MHRK **966.3**
- Gross margin: **7.7%**
- Operating profit: MHRK **42.7**
- Profit before tax: **43.7**
- Net profit: MHRK **35.0**
- Cash flow from operating activities: MHRK **157.6**

Gordana Kovačević, the President of Ericsson Nikola Tesla, commented:

“The extraordinary circumstances, caused by the COVID-19 pandemic that marked the end of Q1 2020, continue. Although during May and June many countries started relaxations of strict measures of movement and distancing, the movement of people and goods is still limited and impacts the global business environment. Since Ericsson Nikola Tesla Group operates globally, these disruptions negatively impact certain part of our business activities. Some customers and partners slowed down or postponed the implementation of contracted projects and reduced their investments. We have also noticed a trend of an increasing number of requests to postpone collection of receivables and new payment models. Our priority is to secure the health and safety of our employees, customers, partners and suppliers, as well as the continuation of stable business performance. Therefore, most of our employees continue to provide services/support to our customers by working remotely, while some of them work from offices. In addition, due to restrictions in travelling our employees cannot carry out some of the activities. In H1 2020, sales revenue increased by 17.6% year-over-year, primarily as a result of taking over the full responsibility for delivering the services of build and maintenance of Hrvatski Telekom's (HT) telecommunications infrastructure (network managed services). The cooperation with HT in radio part of the network, which started with network modernization two years ago, has continued by signing the first 5G agreement in Croatia, making our

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company the exclusive supplier of the radio part of HT's network until 2024. By signing this agreement, HT became one of 99 providers of communication services worldwide that decided to implement Ericsson's 5G technology.

Furthermore, in the operator segment in the domestic market, we continue to provide quality support to our long-term partner A1 Hrvatska in additional modernization and expansion of telecom network.

In the segment of ICT solutions for Industry & Society, we signed a new contract in the field of the Joint Information System of Land Registry and Cadaster (JIS). In the healthcare segment, we have continued the maintenance of the national IT health system - CEZIH.

In export markets, sales revenue is somewhat lower year-over-year, due to the negative impact of COVID-19 on the dynamic of operators' investments. Despite the current circumstances, we continue a good cooperation with the operators HT Eronet (Bosnia & Herzegovina), IPKO (Kosovo), and Crnogorski Telekom (Montenegro). We would like to highlight the continuation of activities on the LTE network expansion for the operator beCloud (Belarus).

The delivery of services to Ericsson has been continuously growing due to new responsibilities, the quality of the performed activities and the competences of our experts in R&D Center, as well as Services and Solutions Expert Centers. Along with the R&D Center's activities on the development of new functionalities, I am proud that our experts were among the first to work on the implementation of 5G networks for Ericsson Corporation. Despite the challenging situation related to COVID-19 and the fact that many employees are working from home, the activities are ongoing as planned.

Looking at the financial indicators at Group level, gross margin decreased to 7.7% as a result of business mix due to taking over the full responsibility for managed services for HT, transformation and restructuring costs, as well as the impact of COVID-19 since March 2020. Operating profit was down by 49% year-over-year, amounting to MHRK 42.7, as a result of lower gross margin and higher selling and administrative expenses. Selling and administrative expenses were higher primarily due to an increased engagement on presales activities related to 4G/5G radio access and core networks, and higher expenses related to managed services with HT. Net profit amounted to MHRK 35.0 and Return on Sales (ROS) was 3.6%. We concluded H1 2020 with a solid balance sheet and an equity ratio of 35.2%. A strong cash flow from operating activities was realized, amounting to MHRK 157.6. At the end of H1, total cash and cash equivalents, including short-term financial assets, amounted to MHRK 290. The Group's Working Capital Efficiency, expressed in Working Capital Days (WCD), was 42 days, and if we exclude services to Ericsson, Working Capital Efficiency was 87 days. Cash conversion rate was 224%.

The project of energy efficiency and the use of renewable energy sources in Ericsson Nikola Tesla, co-financed by the EU from the European Structural and Investment Funds is ongoing as planned, and we expect a successful realization until the end of 2020.

The crisis caused by COVID-19 pandemic clearly shows the important role that telecommunications and introduction of digital services have for the economy and society. We believe that encouraging investments in 5G and digital transformation will have a positive impact on the recovery/development of the economy, attracting investments and speeding up technology innovations, while for the creative individuals it will open opportunities for innovation and business development. In terms of operator segment, the growth of data traffic requires additional customers' investments in networks modernization and expansion in order to secure new services for end-users and high network quality.

The inability to predict the development of the pandemic represents one of the major challenges in risk management. Therefore, we remain focused on detailed business planning, risk monitoring, cost and operating efficiency and we undertake the appropriate measures in order to mitigate the negative impact on our business performance. New circumstances show daily the advantages of digitalization; therefore, the Group's long-term strategy remains unchanged, and the ongoing process of the Company's digital transformation remains one of our

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priority tasks. Our advantage is technology leadership, competent, innovative and motivated employees and partnership with customers. Out of 3200 employees of Ericsson Nikola Tesla Group, 1500 work in the largest Croatian R&D Center that significantly contributes to the development of 5G networks functionalities within the Ericsson's global R&D community. “

## Financial Highlights for the Group:

- Sales revenue amounted to MHRK 966.3 (H1 2019: MHRK 821.7), up by 17.6% year-over-year. Of the total sales revenue, the domestic market accounts for 43.6%, services to Ericsson account for 45.5%, while other export markets account for 10.9%.
- Sales in the Networks segment amounted to MHRK 543 (H1 2019: MHRK 451.7), Digital Services amounted to MHRK 213.7 (H1 2019: MHRK 270.1), Managed Services amounted to MHRK 205.4 (H1 2019: MHRK 98.5), and Emerging Business and Other amounted to MHRK 4.2 (H1 2019: MHRK 1.6).
- Gross profit amounted to MHRK 74.9 (H1 2019: MHRK 108.0), down by 30.7% year-over-year. Gross margin decreased to 7.7% (H1 2019: 13.1%), as a result of business mix due to taking over the full responsibility for managed services for HT, transformation and restructuring costs, as well as the impact of COVID-19 since March 2020 that slowed down a part of our field business activities.
- Selling and administrative expenses increased by 17.6% year-over-year, amounting to MHRK 41.8 (H1 2019: MHRK 35.5), due to higher presales activities related to 4G/5G radio access and core networks, and an increase of expenses related to the project of managed services for HT.
- As a result of lower gross margin and increased selling and administrative expenses, the operating profit decreased by 49.0% year-over-year, amounting to MHRK 42.7 (H1 2019: MHRK 83.7).
- Gain from financial activities decreased to MHRK 1.0 (H1 2019: MHRK 1.4).
- Profit before tax decreased by 48.7% year-over-year, amounting to MHRK 43.7 (H1 2019: MHRK 85.1).
- Net profit was MHRK 35.0 (H1 2019: MHRK 71.1), down by 50.8% year-over-year. Return on sales (ROS) was 3.6% (H1 2019: 8.6%).
- Cash flow from operating activities amounted to MHRK 157.6 (H1 2019: MHRK 32.0). Cash flow was positively impacted by significant collection of receivables from certain customers and lower cash outflow as a result of prolongation of some payments. Cash conversion rate increased to 224% (H1 2019: 23%).
- Working Capital Efficiency, expressed in WCD, was 42 days on Group level (H1 2019: 42 days), and excluding services to Ericsson, Working Capital Efficiency was 87 days (H1 2019: 113 days). The decrease in WCD is a result of high level of realization of previously contracted network modernization projects.
- Total cash and cash equivalents, including short term financial assets, as at June 30, 2020, amounted to MHRK 290 (29.1% of the total assets), while at the end of 2019, they amounted to MHRK 135.8 (14.2% of the total assets). The increase of cash and cash equivalents is the result of strong cash flow from operating activities and additional control of investment activities.
- The company has a solid balance sheet with total assets of MHRK 995.6 as at 30 June 2020, up by 4.3% compared to the end of 2019, primarily due to the increase of total cash and cash equivalents, as a result of a significant collection of current customer receivables and decrease of inventory due to high level of realization of certain network modernization projects. Equity ratio amounted to 35.2% (end of 2019: 33%).

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- With related parties, the transactions were as follows: sales of products and services amounted to MHRK 439.1 (H1 2019: MHRK 255.7), while procurement of products and services amounted to MHRK 181.6 (H1 2019: MHRK 89.5).
- As at June 30, 2020, balances outstanding with related parties were as follows: receivables amounted to MHRK 82.2 (end of 2019: MHRK 116.1), and payables amounted to MHRK 38 (end of 2019: MHRK 95.4).

### Reclassification of financial data:

- Compared to the results published in H1 2019, the Group modified its presentation of Financial Statements to comply with the reporting as per the Capital Market Act (65/18 Article 470). The key changes include Other Group's revenues which were presented last year as the decrease of Direct expenses of sales of products and services, and operating currency exchange which is now presented as Financial income.

### Business situation in major markets

**In the domestic market**, sales revenue amounted to MHRK 421.1 (H1 2019: MHRK 177.0), up by 137.9% year-over-year.

With the strategic partner Hrvatski Telekom (HT), we signed a cooperation agreement at the end of June, which makes us the exclusive supplier of the radio part for HT's mobile network until 2024. By signing this first 5G agreement in Croatia we continue our long-term quality cooperation. The aim of the signed 5G agreement and the continuation of cooperation in radio part of mobile network is to secure higher speeds and 5G coverage for HT's users. Furthermore, we would like to highlight that currently 20 pilot base stations are implemented (Samobor, Zagreb, Krk, Osijek), and intensive activities are ongoing on testing the functionalities and performance of 5G technology, as well as the preparation for commercial operation after the necessary radio frequency spectrum is assigned. The cooperation of HT's and Ericsson Nikola Tesla's experts resulted, for the first time in Croatia, in introduction of the technology of DSS (Dynamic Shared Spectrum) which enables the use of the existing 4G frequencies for 5G technology.

We also continue our strategic cooperation in the field of delivering the services of build and maintenance of HT's telecommunication infrastructure (network managed services), of which we would like to highlight the activities on an intensive build of fiber optics infrastructure for households. In H1 2020, the company Ericsson Nikola Tesla Servisi realized fiber optic infrastructure for 20,000 households and business entities, including 80 percent of the island of Rab, making it the first Croatian gigabit island. Moreover, the activities are ongoing on preparing and implementing the fiber optic infrastructure that will encompass additional 60,000 households and business entities until the end of 2020.

With the strategic partner A1 Hrvatska we have continued the activities on modernization and expansion of radio access network. Ericsson Nikola Tesla secured a high network quality in order for A1 Hrvatska to meet the increased users' demand in the situation caused by COVID-19. We continued the cooperation in the segments of core network and transport telecommunication network, which contributes to the increased network quality and new services for end-users.

Furthermore, A1 Hrvatska put into commercial operation the longest MIMO (Multiple Input – Multiple Output) radio relay network in the world. This was enabled by using Ericsson ML TN system in the configuration 2x2 MIMO at the distance of 26.8 km in the hinterland of the city of Split. Fast implementation and great capacities are the main advantages of connecting base stations in areas where it is not possible or not profitable to build a fixed transport network.

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For the mobile operator Tele2, we have continued to provide support services for voice core network, as well as software solution for data traffic shaping.

In the field of ICT solutions for Industry & Society, a new one-year agreement was signed to upgrade the Joint Information System of Land Registry and Cadaster (JIS). The activities are ongoing on the upgrade of the system of geodetic survey for the State Geodetic Administration, and the 112 system for the Ministry of the Interior of the Republic of Croatia. With the Ministry of Public Administration of the Republic of Croatia, the contracted activities for the introduction of quality management system into Public Administration are ongoing. In cooperation with the Ministry of Health, Croatian Institute for Public Health, we continue the activities of maintenance of the national IT healthcare system - CEZIH.

**In export markets (excluding Ericsson market)**, sales revenue decreased by 8.9% year-over-year to MHRK 105.4 (H1 2019: MHRK 115.8).

The previously mentioned circumstances negatively impacted the dynamic of operators' investments. Some investments were postponed for H2 2020. We continued a good cooperation with the operators HT Eronet (Bosnia and Herzegovina) and IPKO (Kosovo) on the maintenance of their telecommunication networks. With the operator beCloud (Belarus) we continued the activities on the LTE network expansion. With the operator Crnogorski Telekom (Montenegro) the activities continue on the modernization of radio access network.

In ICT segment for Industry & Society, within the project of healthcare system informatization in Kazakhstan, in cooperation with the Ministry of Healthcare of the Republic of Kazakhstan, the activities are ongoing on the maintenance of the national information healthcare system. The activities also continue on healthcare system maintenance for the needs of the Ministry of Healthcare of Armenia.

**In Ericsson market**, sales revenue amounted to MHRK 439.8 (H1 2019: MHRK 529.0), down by 16.9% year-over-year, due to the change of business model regarding managed services of HT's network in 2020. Sales revenue increased by 2.2% for comparable units, excluding managed services.

Ericsson Nikola Tesla's R&D Center successfully continued with ongoing business and projects. Although most of R&D Center's employees work from home, all activities and deliveries are ongoing according to plan.

In radio development, within the business segment Networks, significant functions related to 5G products were delivered. The high quality of these deliveries, as well as continuous work on competence development, resulted in granting new assignment for additional team. In core networks segment, the elements related to modernization and Mobile Switching Center (MSC) virtualization were successfully delivered. Additional responsibilities for the development and maintenance were also achieved in the domain of HLR (Home Location Register). Furthermore, our experts received a great recognition in the beginning of June, when Ericsson Nikola Tesla's R&D Center took over, at Corporate level, the full responsibility for the entire CUDB (Centralized User Database) node, from initial development of functionalities to implementation and maintenance.

Demand for Ericsson Nikola Tesla's experts by Ericsson's global/regional organizations remains high. The impact of COVID-19 pandemic on the realization of activities is limited, since the majority of activities can be performed remotely. Experts from Services and Solutions Center for Networks, along with projects for the customers of Ericsson Nikola Tesla Group, are included in activities of integration and optimization of various technologies for Ericsson customers in the United Kingdom, Germany, Denmark, Finland, Sweden, Greece, Slovenia, Bulgaria, Estonia, Turkey, Singapore, Indonesia, the United Arab Emirates, Bahrain, Qatar, Iraq, Vietnam, Mexico, Albania, Kazakhstan, Pakistan, Brazil, Malaysia, etc. The activities on the development and implementation of software tools for mobile networks management and optimization continues.

Experts from Services and Solutions Center for Digital Services, Media and Operations, along with working on projects for our customers, were also engaged on projects for Ericsson customers in Germany, Sweden,

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Switzerland, the United Kingdom, the Netherlands, Denmark, France, Ireland, Norway, Lithuania, Italy, Slovenia, Poland, Albania and Mexico. They are engaged in complex projects of 5G technology introduction, operational and business support systems, as well as projects of introduction of core solutions in Cloud.

The teams working in IT & Engineering Services unit are achieving excellent results on projects of test environment management and IT operations management. ICT for Industry and Society segment records quality results on projects in the field of IoT platforms and Connected Urban Traffic.

### Other information

At the Annual General Meeting of Ericsson Nikola Tesla joint-stock company, held on 26 June 2020, in special circumstances, among other decisions, a decision was adopted that the Company's net income for the financial year 2019, amounting to HRK 95,551,068.81 will be allocated to retained earnings.

Ericsson Nikola Tesla's major shareholders (as at June 30, 2020)

	Number of shares	% of share capital
Telefonaktiebolaget LM Ericsson	653,473	49,07
Addiko Bank d.d. / Raiffeisen mandatory pension fund, B category	123,514	9.28
OTP banka d.d. / Erste Plavi mandatory pension fund, B category	56,013	4.21
Addiko Bank d.d. / PBZ Croatia osiguranje mandatory pension fund, B category	31,323	2.35
PBZ d.d. / The Bank of New York as Custodian	10,411	0.78
PBZ d.d. / custodian client account	9,759	0.73
OTP banka d.d. /OTP Index fund – open-end alternative investment fund with public offering	8,271	0.62
Addiko Bank d.d. // Raiffeisen voluntary pension fund	8,094	0.61
Zagrebačka banka d.d. / State Street Bank and Trust Company, Boston	4,793	0.36
Vuleta Ivica	4,630	0.35
Other shareholders	421,369	31.64

Share price information in Q2 2020:

Highest (HRK)	Lowest (HRK)	Closing (HRK)	Market cap. (In MHRK)
1,300.00	1,010.00	1,210.00	1,611.3

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Krapinska 45  
Zagreb

OIB: 84214771175

Pursuant to the Articles 462 to 468 of the Capital Market Law (Official Gazette 65/18) the Managing Director of the joint stock company Ericsson Nikola Tesla d.d. Zagreb, Krapinska 45 gives the following:

Statement  
of the Management Board responsibility

The accompanying consolidated and non-consolidated financial statements have been prepared in compliance with the International Financial Reporting Standards (IFRS). The financial statements also comply with the provisions of the Croatian Financial Accounting Law valid as of the date of these financial statements.

Unaudited financial statements for the period January 1, 2020 to June 30, 2020 present a true and fair view of the financial position of the Company and the Group and of the financial performance and cash flows in compliance with applicable accounting standards.

Managing Director:

Gordana Kovačević, MSc

A handwritten signature in black ink, appearing to read "Gordana Kovačević".

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For additional information, please contact:

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For more information about Ericsson Nikola Tesla's business, please visit: <http://www.ericsson.hr>