starman

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CONSOLIDATED MANAGEMENT REPORT

General information

Starman is the biggest cable-TV network based telecommunication company in Estonia. In its activity the company is focused on private customers. This concentration is supported by the entire Starman brand concept, including the company's slogan "Million reasons to stay at home!" Starman's shares are listed on the main list of the Tallinn Stock Exchange.

Until December 2006, when the company launched its ZUUMtv service, Starman only provided services in cities, mostly in densely populated areas. Through its cable network, Starman is currently represented in all major Estonian cities (except Narva), and in all county centres (except Haapsalu, Võru and Kärdla). The company's cable network covers 44% of Estonian households. Starman's triple services (cable television, internet and telephone) are now available to a majority of the company's customers. In Estonia, Starman is the most successful provider of triple services to its cable-TV customers.

Success of Starman continued in 2006. Telephone services rendered a considerable additional impact on the strong market position in the spheres of cable-TV and the internet.

Similarly to previous periods, the company expanded its product selection and enhanced product availability in different areas all over Estonia. While in the beginning of 2005 the company made its first aggressive telephone services campaign, and in the autumn of 2005 the digital television services where launched, the portfolio of Starman was further supplemented in the fourth quarter with the DTT (digital terrestrial television) product. The DTT service is offered in cooperation with AS Levira by a company named Eesti Digitaaltelevisiooni AS and under a separate trademark. The ZUUM trademark was introduced in November and the product was launched at the end of the year. From that date Starman is offering digital television services under two separate trademarks using two different technologies. While digital television services have been offered under the Starman trademark already since autumn 2005, the ZUUMtv is expected to attract a considerable number of new clients especially in those regions of Estonia, where Starman was not present thus far.

In 2006, the company achieved its best ever financial results. Such a good performance can be attributed to both successful investments and sales activities in earlier periods as well as to skilful cost management. The launch of the new product in the fourth quarter entailed substantial additional costs amounting to approximately 0.3 million EUR. With the continued supply of only well-established services the results would have been even better.

Starman's total revenue in 2006 amounted to 15.1 million EUR representing a 24% increase in comparison with the same period of the last year. EBITDA in 2006 amounted to 6.0 million EUR and the net profit attributable to shareholders to 2.8 million EUR, exceeding the relevant figures of the previous year 1.5 and 1.9 times, respectively.

Financial ratios

A selection of ratios for evaluating the economic activities in the year 2006:

	2004	2005	2006
Sales increase	44%	26%	25%
EBITDA margin	32%	33%	40%
Gross margin	12%	15%	21%
Net margin	10%	12%	19%
Revenue/average assets	0.68	0.67	0.72
Equity ratio	51%	54%	58%
Debt to equity	0.73	0.69	0.56
Debt/EBITDA	2.08	1.76	1.19
Investments/EBITDA	2.15	1.16	0.83
Current ratio	0.82	0.67	1.09
Invoice turnover rate (annual)	18.5	20.2	20.0

Definitions:
Sales increase = increase compared to the same period last year
EBITDA = operating profit + depreciation, amortisation and impairments
EBITDA margin: EBITDA / total revenue
Gross margin: operating profit / total revenue
Net margin: net profit attributable to shareholders / total revenue
Equity ratio: total equity / total assets
Debt = borrowings + long-term borrowings
Current ratio: current assets / current liabilities
Invoice turnover rate: period sales / accounts receivable at the end of period

Group structure

Starman Group consists of AS Starman being the parent company and, starting from October 2006, Eesti Digitaaltelevisiooni AS being a subsidiary company. 66% of shares in Eesti Digitaaltelevisiooni AS are held by Starman and 34% of the shares by AS Levira. The financial results of Eesti Digitaaltelevisiooni AS have been consolidated into the Group report line-by-line separately indicating the minority share.

The former subsidiaries of Starman – AS Levi Kaabel, Tallinna Kaabeltelevisiooni AS and AS Telset Telecommunications Group, whose financial results have been consolidated in those of the Group already from June 2004 and with whom the merger agreement was signed in May 2005, were deleted from the Commercial Register in March 2006.

Effect of the general economic environment

Economic growth in Estonia was, undoubtedly, impressive in 2006, compared to most of the other European countries. Domestic consumption was further accelerated by ever-increasing income and favourable credit offers targeted to the retail market. All these factors taken separately had a definite positive effect on Starman's revenue. On the other hand, we must take into consideration that the company is operating in a highly competitive environment where in several segments the further growth potential has shown a continual decrease for the past few years. The quick wage increase and problems with the local labour market where finding qualified labour has become more complicated have had an effect on all Estonian companies. Considering the overall situation in 2006 the company did a good job solving labour market related problems.

Revenue and expenses

As was expected, Starman's total revenue for 2006 showed a modest increase, surpassing yet another landmark – the 15-million-euro limit. Total revenue for the year amounted to 15.1 million euros, i.e. a 3.0-million-euro increase from 2005. Traditionally, cable television and internet services contributed the majority of Starman's total revenue for 2006, accounting for 47% and 35% of the total revenue, respectively. Increasingly emerging telephone services accounted for as much as 16% of the total revenue for the financial year.

Revenue from the cable television services increased by 15% in comparison with the year 2005. Organic growth of the market in recent years has mostly been achieved at the expense of price increase. At the beginning of 2006 the prices of Starman's cable television services further approached those of the countries with a similar living standard but still remain rather low. In addition to the regular price increase, the ARPU (average revenue per user) is also supported by structural changes. As regards structural changes, the triple packages that do not contain smaller programme ranges and the new possibilities such as digital television should be mentioned. In the second quarter of 2006, a new service provider – Elion Ettevõtted AS – entered the market by launching its digital television services. Starman has been active in the highly competitive cable television market for a long time already. Over this time, the company has managed to develop a strong product portfolio which already since autumn 2005 includes also digital television service. The new service provider has not affected the Starman's clientele. At the end of December 2006, the company had a total of 132 thousand cable television customers, 4.0% of which were digital television users (the respective indicators as of the end of December 2005: 130 thousand kroons and 1.2%). The 1.5% annual growth in cable television customer numbers is quite a good result, considering the saturated market and the tightened competitive situation. Monthly fees made up nearly 98% of the total revenue from cable television.

Revenue from the internet services increased 9% year-on-year. At the end of December 2006, the company had 39 thousand internet customers, representing a 26% increase in comparison with the same period a year ago. Starman maintained its position of the leading broadband provider among the private customers in the regions

where the company is present. The current market trend towards higher speeds continues. In the second quarter of 2006, some products were launched which far surpassed the actual needs of the majority of home users. Starman keeps a close eye on the market developments and maintains its position at the forefront of the home user sector in terms of speeds. In line with the general impacts of the market, the ARPU continued to show a downward trend, with the average figure decreasing 14% in comparison with the average of 2005. Starman's popular triple packages in which the internet services are cheaper have a growing impact on the internet ARPU. However, the supporting influence of the triple packages on other services and, hence, also on the average aggregate revenue per user cannot be disregarded. Having increased by 12% from 2005, monthly fees for broadband internet made up 97% of the revenue from internet services. Due to favourable equipment prices, modem rental revenue – a significant source of revenue just a few years ago – has become marginal. While at the end of 2003, the share of customers renting a modem made up 59% of Starman's internet customers, and at the end of 2004, this number was still at a remarkable 24%, modem renting customer numbers dropped to a mere 4% by the end of 2006.

Starman was expecting the telephone service, which was successfully launched the year before, to start having a material positive effect on the company's financial results in 2006. And that is exactly what happened. Telephone services continued to grow rapidly with the revenue exceeding that of the previous year 3.3 times. As of the end of December 2006 the company had 30 thousand telephone clients, i.e. 1.8 times more than at the same time last year. Due to the availability of its own network, good technical solutions and a favourable price policy, Starman has become the only considerable alternative to the incumbent telephone operator Elion Ettevõtted AS which has historically enjoyed its monopoly. In its coverage area, Starman's share of the fixed telephone market for private customers has increased to nearly 22% (10% in the Estonia overall). The average ARPU of the telephone services decreased 2% in comparison with 2005. Call traffic generates most of the revenue from telephone services, with the share of fixed monthly fees amounting to 31% in 2006 (2005: 29%).

Starman views its cable television, the internet and telephone services as a single integrated service. Since the provision of the integrated service has remained a part of the corporate strategy for a long period of time, and the services are designed to support each other, separate analysis of the respective segments might not provide the most accurate overview. In 2006, the total revenue from the given services per client was 25% higher than in 2005.

The launch of the ZUUMtv at the end of the year did not practically have any impact on the Group revenues. At the end of December, Eesti Digitaaltelevisiooni AS had 1.1 thousand customers. Expanding coverage, which by the end of 2007 is anticipated to reach 97% of the Estonian households, and the improving selection of programmes foster expectation of a substantial increase in the number of customers. For Starman, the supply of the new service is similar to the supply of current services, except the transmission services to be supplied by Levira.

The share of revenue generated from sales of goods and materials continued its substantial decrease also in 2006. The sale of various customer equipment (modems and STBs) made up nearly 2/3 of revenue generated of this non-core activity.

In 2006, the operating expenses of Starman amounted to 9.1 million EUR, representing a 12% growth year-on-year. In addition to personnel expenses, the biggest expense items for the year included program fees, marketing expenses, telephone traffic expenses, rental of communication ducts and internet traffic expenses. For the majority of expense items, the rate of growth in expenses was smaller than the increase in revenue. A notable 65% increase in marketing expenses should be attributed to the launch of the ZUUMtv, tight competition and the company's sustained belief in its growth potential. Increase rate of communication ducts rental expenses was one of the main single items which exceeded the increase rate of income. As regards personnel expenses consideration should be given to the fact that the relative share of the company's own activities as opposed to outsourcing has increased in the case of several functions. Therefore, the relative share of outsourced services has declined, which is also manifested in a decrease of several expenditure items year-on-year.

The personnel expenses grew 19% year-on-year. Upon evaluation of personnel costs it should be borne in mind that the given figure encompasses 88% of the company's total payroll whilst the rest is capitalised in accordance with the corporate accounting rules. The average number of employees in 2006 was 210. As of 31 December 2006, the company employed 222 people representing a 7% (14 people) increase in comparison with the end of 2005. The staff has mostly grown on account of part-time employees – at the beginning of 2006 part-time employees formed 9% of the staff but at the end of the year already 16% of the staff. At the end of 2006, the number of employees translated to the full employment equivalent was 199, which is 3% (5 people) higher than at the end of 2005; the average number of employees translated to the full employment equivalent in 2006 was 194. A total of 280 thousand euros was paid in remuneration to the members of the Management Board in 2006, and 21 thousand euros to the members of the Supervisory Board.

As to expenses related to asset valuation, the provision for bad debts amounted to 57 thousand EUR, i.e. to just 0.4% of the period turnover like in 2005. Such a sound level of provisions can be attributed besides efficient credit

risk management to overall favourable situation in economy. In 2006, losses and discounts of inventories amounted to 64 thousand EUR (in 2005, to 72 thousand EUR).

EBITDA—Starman's main performance indicator—amounted to 6.0 million euros in 2006 resulting in an excellent 40% margin. Besides the aggressive growth of telephone services, such a high margin was also upheld by efficient cost management. Eliminating the effect of the just launched ZUUMtv, the EBITDA margin for 2006 is an outstanding 42%.

Depreciation costs increased by 30% in comparison with the year 2005. Owing to the extensive investing activities carried out in recent years, the depreciation costs continued to have a considerable impact on the profit figures.

The net financial result has no significant effect on Starman's overall economic results. The interest expense on external funding used by the company is undoubtedly the single major expense item. These expenses amounted to 0.33 million euros in 2006 — i.e. a 15% increase from 2005. With general trends towards interest rate hikes, the company succeeded in maintaining the average cost of external funding at a reasonable level—the average indicator for 2006 was 4.62%, compared to the 4.32% in 2005.

The net profit attributable to shareholders for 2006 amounted to 2.8 million EUR. Result for minority shareholders - their share from Eesti Digitaaltelevisiooni AS loss - was 0.05 million EUR negative. By making the profit figure comparable with the figure of 2005, i.e. eliminating the income tax in the sum of 0.09 million EUR, the profit of Starman would be double compared to 2005. Eliminating the effect of the just launched ZUUMtv, the net profit margin is an outstanding 21% instead of the "official" 19%.

Balance sheet, investments, financing

In 2006 the company maintained its financial policy which, on the balance sheet, is characterised by high capitalisation, a relatively low debt level and sufficient liquidity.

In 2006, Starman's investments into fixed assets amounted to 5.0 million EUR (in 2005, to 4.7 million EUR), exceeding respective figure of 2005 by 7%. The company made the following investments: 2.2 million EUR in cable network renovation and construction, 0.8 million EUR in telephone modems, 0.7 million EUR in internet equipment (incl. 0.6 million EUR in Head-Ends), 0.5 million EUR in analogue cable television Head-Ends, 0.3 million EUR in STBs (incl. 0.1 million EUR for provision of ZUUMtv) and 0.5 million EUR in other spheres.

Investments in cable network, the company's most important physical asset, increased by 34% compared to 2005. Upgrading and enhancement of the data communication capability of the existing network continued to make up the majority of the investments in the cable network. While at the end of 2005 Starman covered 247 thousand households with 198 thousand – i.e. 80% – of the households being served by a network with the data communication facility, the respective numbers as of 31.12.06 were 251 thousand and 225 thousand (the data communication capability increased to 90%). The company has successfully fulfilled its goals which were established with respect to enhancement of the data communication capability and network modernisation in June 2004 when Starman acquired the TELE 2 cable business and its network where data communication capability was less than 10% and the quality of which mostly did not meet the standards established by Starman. After acquisition of the TELE 2 cable business, the company's data communication capability dropped to 65%, having reached 83% immediately before the transaction. Considering the success of Starman's products, the network reconstruction plans made at the time have been enhanced. In the geographical sense, this means further expansion of triple services and networks data communication capability. Despite extensive real estate development in recent years, the rate of network expansion through construction of a new network has remained modest. Although the network is expanded in accordance with the general market developments, we must take into consideration that the relative rate of growth is low—Starman already covers most of the areas where network construction proves economically feasible. Most of the network investments (over 70%) were made in Starman's most important target area—Tallinn and its vicinity. As regards new network construction, the share of Tallinn and its vicinity is nearly 100%. Major investments outside Tallinn include the upgrading of the Tartu network from the 65% at the beginning of the year to full data communication capability, and the respective reconstruction work in several smaller networks. The company completed the relevant work in Kunda, and for the majority of Pärnu and Jõhvi. At the end of the year, Starman launched the process in Rapla. The company also raised the data communication capability indicator for Kohtla-Järve.

Investments in the telephone modems and STBs are directly related to the growth in the number of customers. This equipment is respectively used by customers for the consumption of telephony and digital television services. In addition to the telephone service, the telephone modem also allows to use the internet service. Investments

into the internet and cable television equipment primarily enhanced quality in the environment of ever growing data communication volumes.

Most of the investments were financed from own resources in 2006. Owner's equity, which as usual has been used for financing a majority of the company's assets, was increased through the profit to reach nearly 13 million euros by the end of the year. For the first time in the last three years the cash flows from principal activity in 2006 outstripped the investment needs, wherefore the total amount of debt remained practically unchanged (having grown by 0.1 million EUR in comparison with the end of the year 2005) and 0.3 million EUR dividend payment was made to shareholders. The company's relative debt level dropped, compared to both equity and cash flow from core business.

Whereas, on the one hand, the creditworthiness of the company has recently improved considerably and, on the other hand, attractive investment plans are still in the perspective (e.g. the DTT service), Starman's current external financing conditions were revised in cooperation with lenders. At the end of September, the company had the majority of its current debts refinanced. As a result, the present average term of debt of 5 years extended to 7 and some of the collaterals were released. In addition, the average interest rate decreased considerably from the previous typical rate of 6-months' EURIBOR +2% to 6-months' EURIBOR + 1%.

Although the year 2006 required extensive investments, Starman's operations still involved only a minor liquidity risk. Considering the specifics of Starman's balance sheet, concentration on single traditional liquidity indicators (e.g. current ratio) can, unfortunately, be misleading. Namely, customer receivables recorded under assets have been significantly undervalued as of the balance sheet date, since the deadlines of a majority of the Group invoices have recently fallen due, and new invoices have not yet been accounted for (the situation is also characterised by a higher-than-average invoice turnover rate). Although the company's day-to-day liquidity position is always normal, Starman maintains an additional liquidity buffer (consisting of cash and short-term debt instruments) for possible short-term setbacks.

High level of inventories as of 31 December 2006 is mainly due to the value of STBs designated for the ZUUMtv offer amounting to 0.5 million EUR in the balance sheet of Eesti Digitaaltelevisiooni AS. Considering the anticipated market capacities for the new product and the delivery schedule of the STBs the level of these inventories will probably remain high also in the future.

Organisation

In the last six years, Starman's turnover has increased by over nine times. Over the years, very quick growth in income has been replaced with a quick growth in income, and thereafter, with modest growth in income. The organisation has reached a more mature stage. With the decrease in expansive tasks, the company has started focusing on keywords such as quality, efficiency and systematisation. Starman's quality management system has been developed and implemented in accordance with the ISO 9001:2000 requirements. In the main quality areas, the company has established concrete indicators which are under continuous surveillance. Some of the most important indicators to mention are service uptime, network quality indicators such as signal levels, signal and noise ratios, customer call reception ratios and service failure elimination speed tresholds. At the same time, in order to remain flexible and competitive in a changing environment, the company tries to conduct its daily operations by also using simple approaches, which are based on the experience gained as a small company. The company continues applying the so-called "thin company" policy. Cost and investment management is based on the principle where areas less related to customer wellbeing are subjected to a significantly stricter monitoring. Differentiating what is important, focusing on the main issues and efficiency are are in forefront, perfection afterwards.

When in 2005 the organisation was put to test with the listing on the Tallinn Stock Exchange and development projects of telephony and digital television, the biggest efforts for 2006 had to do with the establishment of the Eesti Digitaaltelevisiooni AS, launch of ZUUMtv, development of video-on-demand and introduction of changes in the corporate structure. ZUUMtv was launched over a very short period of time after establishment of Eesti Digitaaltelevisiooni AS together with Levira. The fact that the service is provided under the Starman trademark but on behalf of another company placed additional requirements on the available systems, with the company having to create new systems in several cases. With the launch of ZUUMtv, two new distribution channels were implemented for Starman—the company established sales functions and the supporting communication environment for co-operation with electronics stores and Estonian postal service. As regards to video-on-demand, the company launched a pilot project at the beginning of 2007, carefully starting rendering the service while the developing of the service is still in progress. Significant changes were introduced in the corporate structure in 2006, with a majority of the employees being organised into two large divisions – customer service (includes the call centre, customer connection staff and the support functions) and network construction (includes cable network

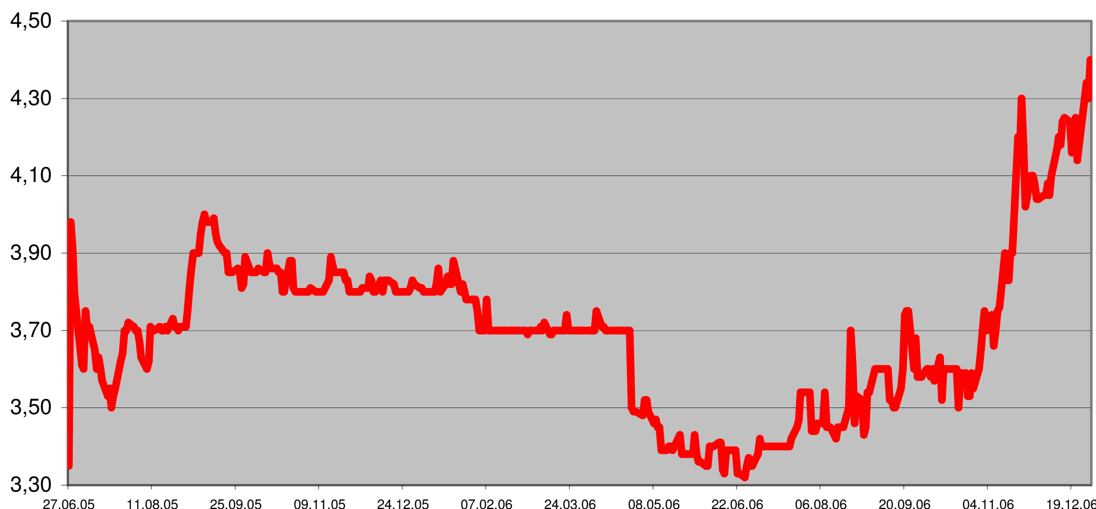
expansion, renovation, and network quality management as well as the support functions). The two large divisions incorporating over 80% of the company's full-time employees are supported by marketing and development, technology and financial units and auxiliary functions such as administration, human resources and legal service. The structural changes were implemented in the 3rd quarter, with first positive results seen already at the end of the year. An organisation is never complete. Therefore, the management keeps a close eye on the changes in main challenges to be faced by the company over time. Further structural changes can not be ruled out, implemented with the purpose of taking up new challenges. Since in addition to the structural changes the number of employees has also shown quite a remarkable increase over the last few years, the company is paying more and more attention to various pursuits of co-operation and search for common goals. Hence the extensive training programme, which was launched in 2005 and taken further in new environment in 2006. The programme will be continued in the future.

Starman's position as a major player on the local retail market was further strengthened in 2006. The new logo and corporate symbolics implemented in the second half of the previous year was further promoted through various brand campaigns. A record number of Starman ads could be seen on TV. In addition to the general brand campaign, this was influenced by ZUUMtv, which was launched at the end of the year as a service to be made available all over the country. The company successfully fulfilled its goal of significantly increasing awareness of the company as a telephone service provider. Successful sales promotion increased awareness of the company’s triple packages (cable television, internet and telephone integrated), which in accordance with their functionality are divided into VIP triple, DIGI triple, HOME triple, MINI triple and MICRO triple package.

Share trading

Starman's shares were listed on the main list of the Tallinn Stock Exchange on 28 June 2005. This was preceded by the IPO, with the company's majority shareholder Royalton Capital Investors putting 3,628,892 shares - i.e. 27.8% of the company's share capital - up for public sale. Simultaneously with the IPO, Royalton Capital Investors sold, at the IPO price, 391,620 shares of the company – i.e. 3.0% of the share capital of the company - to OÜ Com Holding. The IPO was successful – shares were oversubscribed by institutional investors 9.4 times, and by retail investors 3.5 times. The sales price was fixed at 3.35 euros.

Further share price developments until the end of 2006 can be seen in the diagram below:



Some share and trading indicators:

	2005	2006
Number of shares (pcs)	13 053 570	13 053 570
Shares traded (pcs)	2 982 926	3 082 096
Nominal value (EEK)	10	10
Book value (EUR)	0.78	0.97
Closing price at the end of the year (EUR)	3.82	4.40
Highest closing price (EUR)	4.00	4.40
Lowest closing price (EUR)	3.50	3.32
Annual price change, %	14%	15%
Earnings per share (EUR)	0.11	0.22
Dividends (EUR)	0.02	0.04
P/E ratio	34.2	20.4
P/B ratio	4.9	4.5
Dividend yield, %	0.6%	1.0%
Market value (in million of EUR)	49.9	57.4

Definitions:
Book value = owner's equity held by the shareholders of the parent company at the end of the year / number of shares
Annual price change = the difference between the closing price at the end of the year and the closing price at the end of previous year; since no information was available for beginning of 2005, the IPO price was used for the calculation.
Dividend = the dividend paid to shareholder with the allocation of the profit for the year; in case of 2006 it is assumed that dividend is paid according to Management Board's profit allocation proposal
P/E ratio = closing price at the end of the year / earnings per share
P/B ratio = closing price at the end of the year / book value
Dividend yield = dividend / closing price at the end of the year
Market value = number of shares * closing price at the end of the year

At the end of 2006, the company's market value amounted to 57.4 million euros, having increased by 31% compared with the value fixed at IPO. Share trading has been quite unbalanced, partially due to concentration of shares under institutional shareholders not on the selling side and the small liquidity derived from that. The trends which became evident immediately after the IPO (decrease in the share of retail investors) continued in 2006. As of the end of 2006, Starman had 707 shareholders, with shareholders who hold a stake larger than 1% in the company holding a total of 93.0% of the company's share capital (the respective indicators for the end of 2005: 876 shareholders and 90.7%).

As of 31.12.2006, the following shareholders held a stake larger than 1% in the company:

Royalton Capital Investors	- 33.4%
OÜ Constock	- 19.1%
OÜ Com Holding	- 17.8%
Hansa Eastern European Bond Fund	- 7.1%
ING Luxembourg S.A.	- 4.1%
Nordea Bank Finland PLC Clients	- 2.8%
AS Lõhmus Holdings	- 2.6%
Hansa Baltic Growth Fund	- 2.5%
J.P. Morgan Bank Luxembourg S.A	- 2.4%
OKO Bank Plc Client	- 1.1%

The near future

In 2007, Starman will continue making efforts for becoming the best private customer-oriented telecommunication service provider in Estonia.

The Estonian economic growth is expected to remain among the fastest in Europe. The telecommunication sector is bound to benefit from this growth through domestic consumption. Still compared to some previous years the hazards lurking in the economic environment have increased. The company is carefully monitoring the situation with the labour market and domestic consumption where in addition to the expansive activities of local retail banking during recent years money supply can further be increased by the state in order to fulfil the quite daring promises made by politicians during the election campaign. Let us hope that the local economy succeeds in maintaining balance between wage increase and productivity, and the inflation pressure does not seriously create a situation of further postponement of the adoption of the euro.

Our growth expectations for 2007 are similar to those in recent years. All of the main services offered by the company have potential. Still, ZUUMtv, the digital terrestrial television service, could be brought out as the one with the greatest potential.

Income increase will help cable television prices to climb towards the level of other CEE countries where the standard of living is similar, but the prices, considering the purchasing power parities, are still higher than in Estonia. Organic market growth remains limited. Additional opportunities, especially through the growth in ARPU, are offered by the digital television together with several new solutions, such as video-on-demand. We are not expecting the digital television service to make a quick breakthrough - Starman views this service rather from a long-term perspective. The television service launched by Elion Ettevõtted AS already allows us to draw the first conclusions regarding the effect of the increasing competition. There are no visible effects of the launch of the television service over the ADSL network on Starman's activity. Still, we must take into consideration that this technology is quite new, and its effect on the market will rather be seen on a longer perspective.

As regards internet services, we expect the prevailing trends to continue in 2007. The tight competition and the market, which is gradually nearing its saturation point, still allows moderate growth. With constant pressures on internet price, we expect it to decrease – most certainly the price drop will take place on the relative scale (price per data communication unit).

In 2007, Starman will continue promoting itself as a telephone service provider. Although the first two years since the launch of the service have been very successful, we dare not forecast similar figures for the future there should still be sufficient potential for growth in the segment.

In 2007, ZUUMtv will start having a significant effect on the company's financial results. The objective taken with the establishment of Eesti Digitaaltelevisiooni AS was to achieve 50,000 customers in the first two years of operation. Although the launched product was minor to initial plans, we expect through the expansion of coverage area, which is expected to reach 97% of Estonian households by the end of 2007, and improving the programme selection to make up for the initial setback.

Starman’s cable transmission network and customer base provide many further business opportunities. We already discussed video-on-demand above. The company is constantly analysing the market and weighing its resources, thus the possibility of launching additional services/products should not be overlooked.

As regards the EBITDA margin, the year 2006 will probably remain as the all time high for some years to come. This will mainly be conditioned by the launch of ZUUMtv which is a product in its initial stages of development. In the long run the new product is expected to both strengthen the company's market position and profitability. Undoubtedly, the margins in the short perspective are also influenced by the situation on the labour market and some consequent price pressure on several outsourced services.

As regards investments, the investments made by Eesti Digitaaltelevisiooni AS in the STBs required for the use of ZUUMtv will be added to the activities which have played an important role in previous years. In 2007, the company plans to continue extensive network investments. While in earlier periods, network investments mainly meant modernisation, the company will also pursue several projects related to network expansion in 2007. Previous experience in the implementation of such projects, and the successful sales of the company's products allow us to be optimistic. When we add to the above investments the expected growth in customer numbers of core services, and the continual need to invest in product quality in environment of ever-growing datacommunication volumes, we can estimate the volume of investments to remain high also in the near future. Consequently, the effect of depreciation on the company's profit indicators is expected to remain high.

The current absolute level of external financing is mainly sufficient for covering the planned regular investments. A remarkable decrease in the debt to equity ratio may not, however, prove economically reasonable.

Owners may expect dividends, similarly to last year. Again, the company plans to distribute nearly 20% of the profit for 2006 as net dividends.

After years of hard work, Starman has gained a strong position on the Estonian highly competitive telecommunication market. This is the result of the efforts made by our employees. There is still enough room for improvement and Starman has excellent chances of meeting its growing objectives.

CONSOLIDATED FINANCIAL STATEMENTS

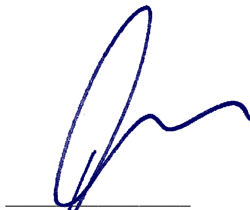
Management representation of the consolidated financial statements

We hereby take responsibility for the preparation of the financial statements set out on pages 10 to 37, and confirm that:

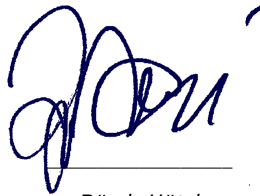
a. the accounting principles used in preparing the consolidated financial statements are in compliance with the IFRS, as adopted by the European Union;

b. the consolidated financial statements give a true and fair view of the financial position of the Group, as well as the results of its operations and cash flows;

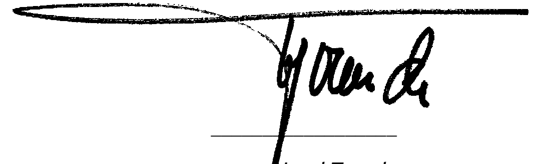
c. the Group and the parent company are able to continue as a going concern.



Peeter Kern
Chairman of the Board



Rändy Hütsi
Member of the Board



Henri Treude
Member of the Board

28 March 2007

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CONSOLIDATED INCOME STATEMENT

in thousands of euros, per annum

	2006	2005	Note
Revenue	15 002	12 031	2
Other income	136	136	3
Goods, raw materials and services	-4 306	-3 869	3
Other operating expenses	-2 243	-2 076	3
Personnel expenses	-2 414	-2 024	3
Depreciation, amortisation and impairments	-2 901	-2 233	10,11
Other operating charges	-135	-183	3
Operating profit	**3 138**	**1 783**	
Net financial items	-295	-324	4
Profit before income tax	**2 844**	**1 459**	
Income tax	-87	0	5
Net profit	**2 757**	**1 459**	
Minority interest	-53	0	
Parent company's share of net profit	**2 809**	**1 459**	
Basic EPS (in EEK)	0,22	0,11	20
Diluted EPS (in EEK)	0,22	0,11	20

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CONSOLIDATED BALANCE SHEET

in thousands of euros, as of December 31

	2006	2005	Note
ASSETS			
Current assets			
Cash	749	282	6
Receivables	787	619	7
Prepayments	188	65	8
Inventories	1 500	760	9
Total current assets	**3 224**	**1 726**	
Non-current assets			
Other financial assets	0	10	
Property, plant and equipment	19 098	17 210	10
Intangible assets	38	26	11
Total non-current assets	**19 137**	**17 246**	
TOTAL ASSETS	**22 360**	**18 971**	
LIABILITIES AND OWNERS' EQUITY			
Liabilities			
Current liabilities			
Borrowings	983	1 071	12
Payables	1 830	1 382	13
Prepayments and deferred income	141	129	14
Total current liabilities	**2 954**	**2 582**	
Non-current liabilities			
Long-term borrowings	6 211	5 997	12
Other long-term liabilities	280	203	14
Total long-term liabilities	**6 491**	**6 200**	
Total liabilities	**9 445**	**8 782**	
OWNERS' EQUITY			
Minority interest	208	0	
Share capital	8 343	8 343	
Legal reserve	167	94	
Retained earnings	4 198	1 753	
Total owner's equity held by the shareholders of the parent company	**12 707**	**10 190**	
Total owners' equity	**12 915**	**10 190**	15
TOTAL LIABILITIES AND OWNERS' EQUITY	**22 360**	**18 971**	

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CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

in thousands of euros, per annum

	Owner's equity held by the shareholders of the parent company						
	Share capital	Share premium	Legal reserve	Retained earnings	**Total**	**Minority interest**	**Total owners' equity**
31.12.2004	**2 781**	**4 375**	**46**	**1 529**	**8 731**	**0**	**8 731**
Bonus issue	5 562	-4 375	0	-1 187	0	0	0
Transfers to legal reserve	0	0	48	-48	0	0	0
Net profit for the financial year	0	0	0	1 459	1 459	0	1 459
31.12.2005	**8 343**	**0**	**94**	**1 753**	**10 190**	**0**	**10 190**
Contributions by minority shareholders	0	0	0	0	0	261	261
Dividends announced	0	0	0	-292	-292	0	-292
Transfers to legal reserve	0	0	73	-73	0	0	0
Net profit for the financial year	0	0	0	2 809	2 809	-53	2 757
31.12.2006	**8 343**	**0**	**167**	**4 198**	**12 707**	**208**	**12 915**

Additional information on transfers to owner's equity has been disclosed in Note 15.

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CONSOLIDATED CASH FLOW STATEMENT

in thousands of euros, per annum

	2006	2005	Note
Cash flow from operations			
Net profit	2 757	1 459	
Adjustments of net profit	3 340	2 465	18
Change in current assets related to operating activities:			
Short-term receivables other than loans and interest, and prepayments	-338	-38	
Change in inventories	-718	-76	
Change in liabilities and prepayments related to operating activities:			
Payables	448	177	
Prepayments and deferred income	89	83	
Total cash flow from operations	**5 578**	**4 070**	
Cash flow from investing activities			
Purchase of tangible and intangible assets	-4 845	-4 178	18
Proceeds on disposals of tangible and intangible assets	179	54	
Investments into subsidiary companies	0	-415	
Disposals of other financial investments	0	209	
Interest received	21	11	
Total cash flow from investing activities	**-4 645**	**-4 320**	
Cash flow from financing activities			
Loan repayments	-48	-48	12
Repayment of finance lease principal	-1 735	-1 195	
Interest paid	-326	-285	
Proceeds from sale and leaseback transactions	1 762	1 464	
Contributions by minority shareholders to owner's equity	261	0	
Dividends paid	-292	0	
Income tax on dividends paid	-87	0	
Total cash flow from financing activities	**-466**	**-64**	
TOTAL CASH FLOW	**467**	**-314**	
Cash and cash equivalents at the beginning of the period	282	595	
Change in cash and cash equivalents	467	-314	
Cash and cash equivalents at the end of the period	**749**	**282**	6

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Note 1 Basis of preparation

General information

The financial statements of AS Starman for the year ended 31 December 2006 were approved with the Resolution of the Management Board on 28 March 2007. Pursuant to the Commercial Code of the Republic of Estonia, the Annual Report, which has been prepared by the Management Board and approved by the Supervisory Board and which also includes the financial statements, shall be approved by the General Shareholders' Meeting. The shareholders shall have the right not to approve the Annual Report prepared and approved by the Management Board, and demand from the Management Board preparation of a new Annual Report.

AS Starman has been registered and is operating in Estonia. The Group includes AS Starman and its subsidiary Eesti Digitaaltelevisiooni AS. Starman owns 66% share in the subsidiary.

The company and its subsidiary employed an average of 210 people in 2006 (2005: 187). The Group's main activity is the provision of cable television and data communication services.

The consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards, as adopted by the European Union, on a historical cost basis, unless otherwise indicated in the accounting principles brought out below. The financial statements have been prepared in thousands of euros. The EMTAK code for business activities of Starman is 6420 – Telecommunication.

Adoption of new and/or changed IFRSs and IFRIC interpretations

The Group has not applied the following IFRSs and IFRIC Interpretations that have been issued but are not yet effective:

- IFRS 7 Financial Instruments: Disclosures (effective for annual periods beginning on or after 1 January 2007). IFRS 7 requires disclosures that enable users to evaluate the significance of the Group's financial instruments and the nature and extent of risks arising from those financial instruments.

- IFRS 8 Operating Segments (effective once adopted by EU, but not earlier than for annual periods beginning on or after 1 January 2009). The standard sets out requirements for disclosure of information about an entity's operating segments and also about the entity's products and services, the geographical areas in which it operates, and its major customers. IFRS 8 supersedes IAS 14 Segment Reporting.

- Amendments to IAS 1 ("Capital Disclosures") (effective for annual periods beginning on or after 1 January 2007). This amendment requires the Company to make new disclosures to enable users of the financial statements to evaluate the Company's objectives, policies and processes of managing capital.

- IFRIC 7 Applying the Restatement Approach under IAS 29 "Financial Reporting in Hyperinflationary Economies" (effective for annual periods beginning on or after 1 March 2006). This interpretation provides guidance on how to apply the requirements of IAS 29 in a reporting period in which an entity identifies the existence of hyperinflation in the economy of its functional currency, when that economy was not hyperinflationary in the prior period.

- IFRIC 8 Scope of IFRS 2 (effective for annual periods beginning on or after 1 May 2006). This interpretation requires IFRS 2 to be applied to any arrangements where equity instruments are issued for consideration which appears to be less than fair value.

- IFRIC 9 Reassessment of Embedded Derivatives (effective for annual periods beginning on or after 1 June 2006). This interpretation establishes that the date to assess the existence of an embedded derivative is the date an entity first becomes a party to the contract, with reassessment only if there is a change to the contract that significantly modifies the cash flows.

- IFRIC 10 Interim Financial Reporting and Impairment (effective for annual periods beginning on or after 1 November 2006). This interpretation establishes that entity shall not reverse an impairment loss recognised in a previous interim period in respect of goodwill or an investment in either an equity instrument or a financial asset carried at cost.

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- IFRIC 11 IFRS 2 – Group and Treasury Share Transactions (effective once adopted by EU, but not earlier than for annual periods beginning on or after 1 March 2007). The interpretation provides guidance on classification of transactions as equity-settled or as cash-settled and also gives guidance on how to account for share-based payment arrangements that involve two or more entities within the same group in the individual financial statements of each group entity.

- IFRIC 12 Service Concession Agreements (effective once adopted by EU, but not earlier than for annual periods beginning on or after 1 January 2008). The interpretation addresses how service concession operators should apply existing International Financial Reporting Standards (IFRSs) to account for the obligations they undertake and rights they receive in service concession arrangements.

The Group expects that the adoption of the pronouncements listed above will have no significant impact on the Group's financial statements in the period of initial application, except for IFRS 7 "Financial Instruments: Disclosures"; IAS 1 amendment Capital Disclosures and IFRS 8 "Operating Segments". The Group is still estimating the impact of adoption of these pronouncements on the disclosures of the financial statements.

The main accounting principles and basis of estimations have been laid out below.

A. Basis of consolidation

The consolidated financial statements comprise the financial statements of AS Starman and its subsidiaries, consolidated on a line-by-line basis. Subsidiaries are consolidated from the date on which control is transferred to the Group, and cease to be consolidated from the date on which the control is transferred out of the Group.

Subsidiaries are companies controlled by the parent company. Control is presumed to exist, if the parent company directly or indirectly holds over 50% of the voting shares of the subsidiary, or is otherwise able to control the operating or financial policies of the subsidiary.

The accounting principles applied by the subsidiary upon preparation of the financial statements are the same principles applied by the parent company. All intra-group transactions, receivables and liabilities, including unrealised profits and losses arising from intercompany transactions, have been eliminated in full. Unrealised losses are not eliminated, if these losses essentially represent impairment in the value of assets.

Minority interest – the share of the subsidiary's profit, loss and net assets which does not belong to the Group, is recorded under a separate entry in the consolidated income statement and balance sheet (under owner's equity).

New subsidiaries are recognised in the consolidated financial statements based on the purchase method. The acquisition cost of subsidiaries is allocated to the fair values of assets, liabilities and contingent liabilities on the acquisition date. The portion of the acquisition cost which exceeds the fair value of the acquired assets, liabilities and contingent liabilities is recognised as goodwill (see accounting principle I). If the fair value exceeds the cost, the difference will immediately be fully charged to the income of the period (under "Other income" in the income statement).

B. Supplementary disclosures on the parent entity of the Group

To comply with the requirements of the Estonian Accounting Law the separate principal reports of parent company should be disclosed together with the consolidated financial statements even though this financial information is not a required part of the consolidated financial statements prepared under International Financial Reporting Standards as adopted by the European Union. The respective disclosure is presented in Notes 23-26. The principal reports of parent company are prepared using the same accounting policies as in the preparation of consolidated financial statements.

In the parent company's unconsolidated balance sheet (Note 24), investments in subsidiaries have been accounted for on a historical cost basis. This means that the investment is initially recognised at acquisition cost, consisting of the fair value of the consideration given, adjusted thereafter by the impairment losses arising from the impairment in the value of the investment. The carrying values of investments will be reviewed when certain events or changes in circumstances indicate the carrying value may not be recoverable. If any such indication exists, the Group makes an estimate of the asset's recoverable amount. If the estimated recoverable amount is smaller than the carrying amount, the investment will be written down to its recoverable amount (the higher of the value-in-use and fair value, less sales expenses). The amount of write-down is charged to the financial expenses of the period.

Dividends paid by the subsidiary are recorded when the parent company's right to receive the dividends (as financial income) is established, except for the portion of dividends payable at the expense of available shareholders' equity generated by the subsidiary before the Group acquires the company. The respective portion of the dividends is recorded as a reduction of the investment.

See accounting principle F for additional information on investments recorded at acquisition cost.

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C. Foreign currency transactions

The Estonian kroon is the functional currency of the parent company, and the reporting currency of the consolidated financial statements of the Group and the unconsolidated financial statements of the parent company. All other currencies are considered foreign currencies.

Transactions denominated in foreign currency are recorded on the basis of the foreign currency exchange rates of the Bank of Estonia officially valid on the transaction date. Assets and liabilities denominated in foreign currency have been translated into Estonian kroons on the basis of the currency exchange rates of the Bank of Estonia officially valid on the balance sheet date.

Foreign exchange gains and losses resulting from revaluation are recorded in the income statement of the reporting period as net financial items.

D. Revenue recognition

Revenue is recognised at the fair value of the received/receivable income. In case of extraordinary payment conditions, revenue is recognised at the net present value of the receivable income.

Revenue from the sales of goods (i.e. hire-purchase of goods) is recognised when all material risks related to the ownership of the asset have been transferred to the purchaser, and the amount of revenue and expenses related to the transaction can be reliably measured. Revenue from the sales of services is recorded upon rendering of the service.

Interest income is recorded on accrual basis, based on the effective interest rate of the asset item. Dividend income is recognised when the respective right of claim arises.

Recognising revenue from connection fees

Connection fees are recognised as the revenue, based on the useful life of the fixed assets related to the connection and on the management's estimates on the period of client relationships. Revenue from connection fees is recorded under revenue within 7 years.

E. Cash and cash equivalents

For the purposes of the cash flow statement, cash equivalents are short-term (with a term of up to three months), highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in market value. Cash and cash equivalents include cash in hand and at bank, cash in transit, short-term deposits with an original maturity of three months or less and money market fund units and units of other funds with equally high liquidity and low interest risk.

F. Financial assets

Financial assets are initially recognised at cost, being the fair value of the consideration given. The acquisition cost includes all expenditures directly related to the purchase of the financial asset, including service charges payable to brokers and advisors, non-refundable taxes and other similar expenditures, except for expenses related to the acquisition of financial assets recognised at fair value in the income statement.

All regular way purchases and sales of financial assets are recognised on the trade date—i.e. the day that the group commits (e.g. concludes a contract) to purchase or sell the particular financial asset item. Regular way transactions are purchases and sales transactions that require delivery of the financial asset to be purchased or sold by the seller to the buyer within the time frame generally established by regulation or convention in the market.

Following initial recognition, financial assets are divided into the following groups:

- Financial assets measured at fair value in the income statement (shares held for trade and bonds which are not intended to be held to maturity, as well as other securities and derivative instruments with a positive value);
- investments intended to be held to maturity (bonds which have a fixed maturity date and are intended to be held to maturity);
- loans and receivables (loans granted, accounts receivable and other receivables);available for sale financial assets (all other financial assets not specified above).Subsequent to initial recognition, financial assets are measured at their fair value, except for:

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a. receivables, which the group has not purchased for resale, or financial assets intended to be held to maturity by the group are measured at amortised cost;

b. investments in shares and other equity instruments the fair value of which cannot be reliably measured (incl. derivative instruments related to such assets) are recognised at cost.

Financial assets measured at fair value

Financial assets that are measured at fair value are revaluated on each balance sheet date into their fair value, which includes the possible transaction costs related to the disposal of the asset. The fair value of listed securities is based on the closing price of the security, as well as the official exchange rate of the Bank of Estonia on the balance sheet date. Unlisted securities are measured at their fair value on the basis of the information available to the group on the value of the investment.

For the assets accounted in the category of financial assets measured at fair value in the income statement, gains and losses from changes in fair value, proceeds and losses from disposals of financial assets measured at fair value, as well as interests and dividends on the respective securities, are recognised under "Net financial items" in the income statement.

Available for sale financial assets are measured at fair value, except for investments in shares and other equity instruments the fair value of which cannot be reliably measured, and which are measured at cost. Any gains and losses arising from changes in the fair value of available-for-sale financial assets are recorded under "Revaluation reserve" in owner's equity. The revaluation reserve is charged to the income statement upon disposal of assets or drop in the value of assets. The impairment loss reclassified from owner's equity to the income statement is the difference between the acquisition cost (less any principal repaid, and amortisation) and the current fair value of the financial asset, less any impairment losses of the financial assets previously measured in the income statement.

Receivables and financial assets intended to be held to maturity

Receivables, which the group has not purchased for resale, including financial assets that are intended to be held-to-maturity are measured at amortised cost using the effective interest rate method. Amortised cost is calculated by taking into account any discount or premium on acquisition, as well as expenses directly related to the transaction, over the year to maturity.

Financial assets measured at amortised cost will be written down, if it is probable that their recoverable amount is lower than their carrying amount. The recoverable amount of a financial asset measured at amortised cost is the net present value of future cash flows from the financial asset, discounted, upon its initial recognition, with the effective interest rate. The write-down of financial assets related to operating activities is charged to expenses in the income statement (under "Other operating expenses") while the write-down of financial assets related to investing activities is charged to financial expenses in the income statement.

Impairment of financial assets will be presented separately for each item, if the item is material. If evaluation of receivables on individual basis proves impossible, only the material receivables will be evaluated. Other receivables are evaluated as a set of receivables, considering the information available regarding the customer's previous debts. Accounts receivable, whose collection proves impossible or financially unreasonable, are deemed bad debts and are written off from the balance sheet. The allowance will be established for doubtful receivables earlier, if certain events indicate that the recoverable amount of the receivable has fallen below its carrying amount.

In case of collection of receivables previously written down, or other events indicating that the write-down is no longer justifiable, the previous write-down will be reversed in the income statement as a reduction of the expense item to which the write-down was initially charged.

Financial assets measured at acquisition cost

Financial assets measured at acquisition cost will be written down to their recoverable amount, if the recoverable amount has fallen below the carrying amount. The recoverable amount of financial assets measured at cost consists of the estimated future cash flows from the financial asset, discounted with the average rate of return from similar financial assets on the market. The amount of write-down is charged to the financial expenses of the period.

The derecognition of financial assets will take place when the group no longer controls the right over the cash flows attributable to the financial asset, or when the cash flows attributable to the asset, and a majority of the risks and benefits related to the financial asset are transferred to a third.

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G. Inventories

Inventories are recorded at acquisition cost, consisting of the purchase price, customs duties, other non-refundable taxes and direct transportation costs related to the purchase, less possible discounts. The acquisition cost of inventories is calculated by using the weighed average acquisition cost method.

Inventories are measured in the balance sheet according to the lower of the acquisition cost or net realisable value. The amount of write-down of inventories to their net realisable value is recorded as expenses of the reporting period, under “Goods, raw materials and services”.

H. Property, plant and equipment

Assets with expected useful life of more than one year are capitalized as fixed assets, if it is probable that future economic benefits associated with the asset will flow to the enterprise.

PPE are recorded at cost, consisting of the purchase price and expenditures directly related to the acquisition.

Following initial recognition, an item of PPE is carried in the balance sheet at its cost, less accumulated depreciation and any accumulated impairment losses. If the recoverable amount of the non-current asset item drops below its carrying amount, the asset will be written down to its recoverable amount (the higher of the fair value, less sales expenses, or the value-in-use). Impairment tests will be conducted, if there is any indication that the carrying amount may not be recoverable. The write-down is charged to the expenses of the period, under "Other expenses" in the income statement.

On each balance sheet, the group assesses whether there is any indication that the previous impairment is no longer justified. If there is any such indication, the group will assess the recoverable amount and, if necessary, reverse the previous write-down. The reversal of the write-down is recorded as a reduction of the expenses during the period when the reversal occurred.

Expenses incurred on PPE after their recognition (e.g. replacement of a part of the asset item) are added to the book value of the item, provided it meets the following criteria: (a) the asset item is likely to generate economic benefits for the group in the future; and (b) the acquisition cost can be reliably measured. Replaced parts are written off from the balance sheet. All other costs are charged to the expenses of the period when incurred.

If the PPE item consists of distinguishable components with different useful lives, these components are separately recorded under assets, and their depreciation rates specified separately thereof in accordance with their useful lives.

Depreciation of PPE is calculated on a straight-line basis. Depreciation rates are determined for each PPE item individually, depending on its useful life.

The following annual depreciation rates apply for PPE groups:

- Buildings and facilities 2.5%
- Cable transmission networks 8%
- Head-Ends 12.5-14.29%
- Modems 20-25%
- STBs 20%
- Machinery and equipment 20-25%
- Other equipment; fixtures, fittings and tools 20-40%
- Equipment used for service provision 16.67-50%

Land is not depreciated.

PPE will no longer be depreciated if its residual value (i.e. the amount the group would currently receive, if the PPE were as old as and in the same condition as it is estimated to be at the end of its useful life) exceeds its carrying amount.

The depreciation methods, depreciation rates and residual values of PPE are reviewed at least at the end of each financial year. If the new figures differ from previous figures, the changes will be recorded as changes in accounting estimates (prospectively).

PPE is derecognised upon disposal of the asset, or if the company can expect no financial benefits from use or disposal of the asset. Any profits and losses arising from derecognition of PPE are charged to "Other income" or "Other expenses" in the income statement of the period when the PPE were derecognised.

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PPE items which are likely to be sold within 12 months are reclassified into held for sale non-current assets, and recorded on a separate entry under current assets in the balance sheet. Held for sale non-current assets will no longer be depreciated, and will be recorded at the lower of the net book value or fair value (less sales expenses).

I. Intangible assets

Intangible assets acquired separately from a business combination will be recognised only if the following conditions are met:

a. the asset item is controlled by the group;

b. generation of future economic benefits from the object is likely;

c. the acquisition cost of the item can be reliably measured.

Intangible assets acquired from a business combination will be recognised separately from goodwill, if the asset items are distinguishable or arise from contractual or other legal rights, and their fair value can be reliably measured on the date of acquisition.

Intangible assets are initially recorded at acquisition cost, consisting of purchase price and expenses directly related to the acquisition. Following initial recognition, an item of intangible assets is carried in the balance sheet at its cost, less accumulated amortisation and any accumulated impairment losses.

The useful lives of intangible assets are assessed to be either infinite or definite. Amortisation of intangible assets with a definite useful life is calculated on a straight-line basis. The following annual amortisation rates are used:

- Purchased licenses, trade marks and similar items 20-33%

Amortisation of intangible assets with a definite useful life is recorded under "Depreciation, amortisation and impairments" in the income statement. The amortisation period and amortisation methods of definite intangible assets are reviewed at the end of each financial year. Changes in estimated useful life or future economic benefits over time are recorded as changes in the amortisation period and amortisation methods (i.e. as changes in accounting estimates).

If there is any indication that the recoverable amount of definite intangible assets has fallen below its carrying amount, the asset will be tested for impairment and, if necessary, written down to its recoverable amount (see accounting principle H).

Infinite intangible assets are tested for impairment annually either individually or at the cash generating unit level. These intangible assets are not amortised. The useful life of infinite intangible assets is reviewed on an annual basis to make sure the useful life has remained infinite. Adjustments, where applicable, are made on a prospective basis.

<u>Research and development costs</u>

Research costs are expensed as incurred. Intangible assets from development projects are recognised as assets only if the group is able to validate (1) its technical capacities for making the assets available for use or sale; (2) its intent to complete the development project and the ability to use or dispose of the asset; (3) availability of future economic benefits from the asset; (4) availability of financial resources for completing the development project; and (5) that the costs related to the development project can be reliably measured.

Following initial recognition, development projects are measured at cost, less accumulated amortisation and any accumulated impairment losses. Any expenditure carried forward is amortised over the year of expected future sales from the related project.

The assets related to the development projects will be tested for impairment on an annual basis, until the development project is available for use or sales. The assets will be tested for impairment more frequently, if there is any indication of a drop in their value.

<u>Goodwill</u>

Goodwill is initially measured at cost, being the excess of the cost of acquisition over the fair value of the acquired net assets, liabilities and contingent liabilities on the date of acquisition. Following initial recognition, goodwill is measured at cost, less any accumulated impairment losses. Goodwill is reviewed for impairment annually or more frequently, if events or changes in circumstances indicate that the carrying value may be impaired.

In order to determine the impairment, any goodwill acquired is allocated to each cash-generating units expected to benefit from the combination's synergies, or groups of such units. Allocation of goodwill between cash-generating units is based on intra-

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group reporting—goodwill is allocated to the lowest level, where it is monitored by the management within the framework of internal accounting.

Impairment is determined by assessing the recoverable amount of the cash-generating unit, to which the goodwill relates. Where recoverable amount of the cash-generating unit is less than the carrying amount, an impairment loss is recognised. Impairment losses are recorded as expenses under "Depreciation, amortisation and impairments" in the income statement. Impairment losses will not be reversed, if the recoverable amount of goodwill rises above its carrying amount (see accounting principle H).

J. Financial liabilities

Financial liabilities are initially recognised at their acquisition cost, consisting of the fair value of the amounts received thereof. Following initial recognition, financial liabilities are measured at their amortised cost by using the effective interest rate method.

Interest expenses related to the financial liability are charged to the expenses of the period on accrual basis under "Net financial items" in the income statement.

The financial liability will be derecognised when the liability is paid, cancelled or expired.

K. Provisions and contingent liabilities

Provisions are recognised in the balance sheet when the group has a present obligation (legal or constructive) as a result of a past event; it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. The management's judgements and experience as well as evaluations of independent experts (if necessary) are taken as basis for evaluating the provisions. The provisions are recorded in the balance sheet in the amount required to settle the obligation as at the balance sheet date.

Promises and other commitments that in certain circumstances may become liabilities, but only have a lower than 50% probability of becoming liabilities (according to the management of the company), are disclosed as contingent liabilities in the notes to the financial statements.

L. Corporate income tax

Pursuant to the Income Tax Act, Estonian companies are not subjected to pay income tax on the profit. Rather, they are subjected to income tax on the paid dividends. The established tax rate was 23/77 on the net dividend paid until 31 December 2006 and 22/78 from 1 January 2007 onwards. Pursuant to the valid Income Tax Act, the income tax rate will be lowered by 1% a year to 20/80 on the net dividend paid after 1 January 2009. Since income tax is paid on the dividends rather than profit, all temporary differences between the tax bases and carrying values of assets and liabilities cease to exist.

The company's potential income tax liability related to the distribution of its retained earnings as dividends is not recorded in the balance sheet. The maximum possible tax liability related to the payment of the company's retained earnings as dividends is disclosed in Note 15.

Income tax from payment of dividends is recorded under expenses in the income statement at the moment of announcing the dividends.

The payable income tax is recorded under current liabilities.

M. Legal reserve

Pursuant to the Commercial Code of the Republic of Estonia, at least 5% of the net profit must be transferred to the legal reserve each financial year, until the legal reserve amounts to at least 10% of the share capital. The legal reserve cannot be paid out as dividends. Still, it can be used for covering the loss, if loss cannot be covered from the available shareholder's equity. Legal reserve can also be used for increasing the share capital of the company.

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N. Accounting for lease

Lease transactions, where all material risks and benefits from ownership of an asset are transferred to the lessee, are treated as finance lease. All other lease transactions are treated as operating lease.

Assets leased under finance lease are recorded in the lessee's balance sheet at the lower of acquisition cost or the net present value of minimum lease payments. The depreciation period of assets acquired under finance lease is the useful life of the asset item. Assets leased out under finance lease are recorded in the balance sheet as a receivable in the amount of the net investment in the finance lease. Rental payments are divided into financial expenses and income, and rental payable/receivable so that the interest rate would be the same at any given moment.

In case of operating lease, the assets are recorded in the lessor's balance sheet. Operating lease payments are recorded during the lease period as income (by lessor) and expenses (by lessee) based on the straight-line method.

O. Derivative instruments

Derivatives (forward, future, swap or option contracts) are measured in the balance sheet at fair value by using a quotation. Derivative instruments will be recorded under assets, if their value is positive, and under liabilities, if value is negative. Gains and losses arising from the revaluation are recorded under "Net financial items" in the income statement. The differences between the exercise exchange rates of the derivatives and respective exchange rate of Estonian Bank on the settlement date are recorded in the profit and loss statement as “Other” under “Other income”/”Other expenses”.

P. Share-based payment transactions

Employees (including senior executives) of the Group receive remuneration in the form of share-based payment transactions, whereby employees render services as consideration for equity instruments.

In situations where some or all of the goods or services received by the entity as consideration for equity instruments cannot be specifically identified, they are measured as the difference between the fair value of the share-based payments and the fair value of any identifiable goods or services received at the grant date.

The cost of equity-settled transactions with employees is measured by reference to the fair value at the date on which they are granted. The fair value is determined by an external valuer using an appropriate pricing model, further details given in note 20.

The cost of equity-settled transactions is recognized, together with a corresponding increase in equity, over the period in which the performance and/or service condtions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award (the vesting date). The cumulative expense recognized for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Group’s best estimate of the number of equity instruments that will ultimately vest. The income statement charge or credit for a period represents the movement in cumulative expense recognized as at the beginning and end of that period.

No expense is recognized for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether or not the market condition is satisfied, provided that all other performance conditions are satisfied.

Where the terms of an equity-settled award are modified, the minimum expense recognized is the expense if the terms had not been modified. An additional expense is recognized for any modification, which increases the total fair value of the share based payment arrangement, or it is otherwise beneficial to the employee as measured at the date of modification.

Where an equity-settled award is cancelled, it is treated as if it had vested on the date if cancellation, and any expense not yet recognized for the award is recognized immediately. However, if a new award us substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paraghaph.

The dilutive effect of outstanding options is reflected as additional share dilution in the computation of earnings per share (further details given in note 20).

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R. Segment reporting

Starman views the services rendered by the company as an integral whole. The corporate strategy and investment policy has been developed on the basis of the established cable transmission network so as to render as many combined services as possible. Since operating expenses and investments have been recognised based on the above factors, their division into separate services with the purpose of getting an accurate overview of segment profitability or an accurate balance sheet proves impossible. The company operates only in the Republic of Estonia. Considering Starman's turnover and the total market volume, the management believes it would prove unreasonable to view different geographical areas as different segments.

S. Use of estimates in the preparation of financial statements

The preparation of financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, income and expenses and disclosure of contingencies. The significant areas of estimation used in the preparation of these financial statements relate to accruals, depreciation and impairment evaluation. Future events may occur which may cause the assumptions used in arriving at the estimates to change. The effect of any changes in estimates will be recorded in the financial statements, when determinable.

T. Events after the balance sheet date

Material circumstances that have an effect on the valuation of assets and liabilities and became evident between the balance sheet date and the date of preparing the financial statements, but are related to transactions that took place in the reporting period or earlier periods, are recorded in the financial statements.

Subsequent events that have not been taken into consideration when valuating the assets and liabilities but have a material effect on the result of the next financial year, are disclosed in the financial statements.

Note 2 Revenue

in thousands of euros, per annum

AS Starman Group's revenue for 2006 and 2005 was fully generated on the Estonian market, and divided into the following fields of activity:

Fields of activity	**2006**	**2005**
Cable television services	7 160	6 210
Internet services	5 242	4 817
Telephone service	2 358	721
Sales of goods and materials	239	282
DTT services*	3	0
Total	**15 002**	**12 031**

*DTT – Digital Terrestrial Television

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Note 3 Other income and expenses

in thousands of euros, per annum

	2006	2005
Other income		
Gains on disposals of non-current assets	10	15
Revenue from fines for delay	89	78
Revenue from client prepayments	25	24
Other	12	19
Total other income	**136**	**136**
Goods, raw materials and services		
Services purchased	-3 828	-3 291
Materials	-64	-66
Goods purchased for resale	-175	-233
Maintenance expenses	-176	-207
Other	-64	-72
Total goods, raw materials and services	**-4 306**	**-3 869**
Other operating expenses		
Consulting and advisory expenses	-192	-343
Marketing expenses	-1 028	-624
Customer information expenses	-301	-340
Office expenses	-235	-269
Allowance for doubtful receivables	-57	-53
Transportation expenses	-209	-174
Other	-222	-273
Total other operating expenses	**-2 243**	**-2 076**
Personnel expenses		
Wages and salaries	-1 807	-1 510
Social tax	-607	-513
Total personnel expenses	**-2 414**	**-2 024**
Other expenses		
Fringe benefit tax on options	0	-115
Other*	-135	-67
Total other expenses	**-135**	**-183**

* In 2006, other expenses include a realised loss in the amount of 114 thousand EUR from forward transactions for purchasing US dollars. Said forward transactions were mostly entered into at the end of 2005 for covering short USD positions. Whilst USD has depreciated in comparison with the exchange rate prevailing at the time of concluding the transactions, the company has gained from lower operating expenses (mostly concerns the item “Services purchased”) and from being able to make investments on more favourable terms. The last forwards matured in the fourth quarter of 2006.

Note 4 Net financial items

in thousands of euros, per annum

	2006	2005
Interest expenses and -income	-305	-275
Foreign exchange gains/losses	16	-44
Other financial expenses	-5	-6
Total net financial items	**-295**	**-324**

Note 5 Income tax

The group's income tax expense for 2006 in the amount of 87 thousand euros (2005: zero euros) is made up of income tax calculated on dividends (see Note 15).

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Note 6 Cash

in thousands of euros, as of December 31

	2006	2005
Cash in hand and at bank	682	262
Cash in transit	67	19
Total cash and cash equivalents	**749**	**282**

Note 7 Receivables

in thousands of euros, as of December 31

	2006	2005
Trade accounts receivable	862	686
Allowance for doubtful receivables[1]	-110	-89
Other short-term receivables	35	22
Total receivables	**787**	**619**

[1] The following changes occurred in the allowance for doubtful receivables (per annum):

	2006	2005
Balance at the beginning of the period	**-89**	**-65**
Additional write-down (see Note 3)	-57	-53
Uncollectible receivables written off from the balance sheet	36	29
Balance at the end of the period	**-110**	**-89**

Note 8 Prepayments

in thousands of euros, as of December 31

	2006	2005
Prepaid taxes	139	0
Prepaid services	49	65
Total prepayments	**188**	**65**

Prepaid taxes include VAT prepayment of Eesti Digitaaltelevisiooni AS. See Note 13 for taxes payable.

Note 9 Inventories

in thousands of euros, as of December 31

	2006	2005
Raw materials	756	465
Goods and customer equipment purchased for resale	744	295
Prepayments for inventories	0	1
Total inventories	**1 500**	**760**

A total of 54 thousand euros of inventories were written down in 2006 (2005: 51 thousand euros) in connection with the drop of the acquisition cost of goods purchased for resale below their net realisable value (sales price, less expenses incurred for the purpose of making the products available for sale, and selling the products).

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Note 10 Property, plant and equipment

in thousands of euros

	Land and buildings	Machinery and equipment	Other non-current assets	Prepayments	Total PPE
Net book value 31.12.2004	**13 446**	**1 358**	**120**	**0**	**14 924**
Purchases and additions	2 437	2 138	72	0	4 647
Reclassification[1]	0	-100	-9	0	-109
Sales	-31	-3	0	0	-34
Depreciation charge	-1 516	-657	-44	0	-2 217
Net book value 31.12.2005	**14 336**	**2 736**	**138**	**0**	**17 210**
Purchases and additions	2 849	1 988	56	69	4 962
Reclassification	0	-22	0	0	-22
Sales	-169	0	0	0	-169
Depreciation charge	-1 733	-1 098	-52	0	-2 882
Net book value 31.12.2006	**15 283**	**3 604**	**142**	**69**	**19 098**

As of 31.12.2005					
Acquisition cost	19 833	4 388	362	0	24 583
Accumulated depreciation, amortisation and impairments	-5 498	-1 652	-224	0	-7 373
As of 31.12.2006					
Acquisition cost	22 363	6 337	418	69	29 186
Accumulated depreciation, amortisation and impairments	-7 079	-2 733	-275	0	-10 088

1 Reclassification involves the transfer of machinery and equipment and other non-current assets to assets, under "Goods, raw materials and services".

As of 31.12.2006, the acquisition cost of fully amortised non-current assets still used by the company amounted to 1,083 thousand euros (2005: 582 thousand euros). The acquisition cost of non-current assets written off in 2006 amounted to 118 thousand euros and net book value to 0 euros (2005: 536 thousand and 0 euros). Information on PPE items established as collateral to borrowings has been disclosed in Note 12.

Note 11 Intangible assets

in thousands of euros

	Licences	Total intangible assets
Net book value 31.12.2004	**20**	**20**
Purchases and additions	16	16
Reclassification	5	5
Amortisation charge	-16	-16
Net book value 31.12.2005	**26**	**26**
Purchases and additions	31	31
Amortisation charge	-19	-19
Net book value 31.12.2006	**38**	**38**

As of 31.12.2005		
Acquisition cost	57	57
Accumulated depreciation, amortisation and impairments	-31	-31
As of 31.12.2006	**Licences**	**Total intangible assets**
Acquisition cost	87	87
Accumulated depreciation, amortisation and impairments	-49	-49

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Note 12 Borrowings

in thousands of euros, as of December 31

2006	Current portion	Non-current portion		Total borrowings
		1-5 years	over 5 years	
Long-term bank loans[1]	48	191	0	239
Finance lease liability[2] (Note 16)	935	5 155	865	6 955
Total borrowings	**983**	**5 346**	**865**	**7 194**

2005				
Long-term bank loans[1]	48	239	0	287
Finance lease liability[2] (Note 16)	1 023	5 754	3	6 780
Total borrowings	**1 071**	**5 997**	**0**	**7 067**

[1] In 2002, the company concluded with Nordea Bank Finland Plc Estonia Branch a new loan agreement to replace the previous overdraft agreement. The loan, in the initial amount of 415 thousand euros, has been denominated in euros and has an interest rate of 6-month Euribor+2%. The loan will be repaid in equal monthly instalments, with the consideration that, upon maturity of the loan term in 2009, the last instalment would amount to 131 thousand euros.

AS Starman has established a 1st-rank mortgage in the amount of 288 thousand euros on the company's real estate located at Akadeemia tee 28 in Tallinn as a collateral to the long-term loan from Nordea Bank Finland Plc. Estonia Branch. As of 31.12.2006, the net book value of the real estate amounted to 452 thousand euros (31.12.2005: 451 thousand euros). In addition, the company has established a 1st-rank commercial pledge on AS Starman's immovables in the amount of 141 thousand euros as a collateral to the above loan.

[2] Finance lease transactions are secured by the leased assets, except for one transaction, where the company has established for the benefit of SEB Ühisliising AS a 2nd-rank commercial pledge on AS Starman's immovables in the amount of 767 thousand euros.

Note 13 Payables

in thousands of euros, as of December 31

	2006	2005
Trade accounts payable	1 048	662
Taxes payable[1]	367	272
Employee-related liabilities	232	189
Other payables	183	259
Total payables	**1 830**	**1 382**

[1] Taxes payable are divided as follows:

	2006	2005
VAT	164	98
Social tax	112	89
Withheld income tax	82	76
Other taxes	9	8
Total taxes payable	**367**	**272**

See Note 8 for prepaid taxes.

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Note 14 Prepayments and deferred income

in thousands of euros, as of December 31

	2006	2005
Prepayments received[1]	95	96
Deferred income[2]	47	34
Total prepayments	**141**	**129**

[1] Prepayments received consist of prepayments received from customers for goods and services in the course of daily business operations.

[2] Deferred income consists of subscription fees, which are to be charged to income over a term of 7 years. As of 31.12.2006, the long-term portion in the amount of 280 thousand euros (2005: 203 thousand euros) has been recorded under "Other long-term liabilities" in the balance sheet.

Note 15 Owner's equity

The company's share capital amounts to 130,535,700 EEK (8,342,752 EUR), and is divided into a total of 13,053,570 registered common shares with a nominal value of 10 EEK. All shares have been fully paid for. The maximum number of shares allowed by the Articles of Association is 21,052,800, and the minimum number is 5,263,200.

Pursuant to the articles of association, the company's supervisory board has the right to increase the share capital by 440,990 EEK (i.e. by 5.3%) within 3 years after the introduction of amendments to the articles of association on 17 May 2005. The supervisory board can exercise this right for realisation of the stock options granted to the management (see Note 20). The resolution of the shareholders' meeting held on 17 May 2005 excludes the shareholders' preferential right to subscribe for shares subjected to the option scheme.

In accordance with the resolution of the annual general meeting of shareholders held on 25 May 2006, 20% of the net profit for the year 2005, i.e. EUR 0.022 per share, was paid to shareholders as net dividends on 21 June 2006. Starman paid 292 thousand EUR in net dividends, transferred 73 thousand EUR into the legal reserve, and retained the rest of the profit. As a result, the company incurred income tax expenses in the total amount of 87 thousand euros. This amount has been charged to the expenses of the period (see Note 5). No dividends were announced in 2005. The Management Board has made a proposal of announcing dividends in 2007 in the amount of 0.045 EUR per share – i.e. approximately 20% of the net profit for 2006. The company will thus announce dividends in the amount of 584 thousand euros, incurring an income tax liability in the amount of 165 thousand euros.

The company's potential income tax liability

As of 31.12.2006, the group's retained earnings amounted to 4,198 thousand euros. After the 140-thousand-euro transfer to legal reserve, the maximum possible income tax liability related to the payment of the company's retained earnings as dividends is 893 thousand euros. The company can thus pay 3,165 thousand euros in net dividends.

The maximum possible income tax liability has been calculated based on the assumption that the net dividends to be paid, and the related total income tax expenses would not exceed the distributable profit as of 31.12.2006.

Note 16 Finance lease and operating lease

The group has made investments into cable networks, machinery and equipment under finance lease (see also Note 10), incurring the following liabilities from these transactions (as of December 31, in thousands of euros):

	2006	2005
Current portion - payable within 1 year	935	1 023
Non-current portion - payable within 1-5 years	5 155	5 754
Non-current portion - payable in over 5 years	865	3
Total finance lease liability (Note 12)	**6 955**	**6 780**
Repayment due date	2013	2011
Interest rate	4.6-5.2%	4.1–6.2%
Underlying currency	EEK, EUR	EEK, EUR

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Contents, terms and conditions of sales and leaseback transactions

The company has raised most of it's external funding through some major sales and leaseback transactions. For partial financing of the construction of Tartu cable transmission network AS Starman sold with two transactions to Ühisliisingu AS the cable television Head-End and a part of the cable transmission network for a total of 697 thousand euros, and leased back the sold non-current assets on finance lease terms for a total of 488 thousand euros thereafter. In the same year, the company sold its cable television Head-End in Tallinn, as well as a part of the cable transmission network in Tallinn and its vicinity to Ühisliising for a total of 2,564 thousand euros, and leased back the non-current assets on finance lease terms for a total of 1,278 thousand euros thereafter, using the acquired funds mainly for purchasing of 40% of the shares of Starman Internet. In connection with this transaction, a 2nd-rank commercial pledge was established on the movable property of AS Starman for the benefit of Ühisliisingu AS in the amount of 767 thousand euros. In 2004, the company financed the acquisition of TELE 2 cable business (purchase of subsidiaries) when, on 1 June 2004, Starman sold the cable transmission network acquired, for the most part, from TELE 2 for 4,282 thousand euros, and leased back the sold non-current assets on finance lease terms for 3,835 thousand euros thereafter. Effectively, the given agreement was associated with the above agreements through various additional conditions (e.g. joint collateral) for uniting the transactions into an integral whole. Joint payment conditions were thus established for all transactions - incl. a 7-year payment schedule, interest rate of 6-month Euribor + 2% and the 2.5 years grace period when only the interest is payable.

As of 31.12.2005, the total finance lease balance of all the above transactions amounted to 4,911 thousand kroons in the balance sheet. Starman has also used other small-volume sales and leaseback transactions for financing purposes, but these do not, in effect, differ from standard finance lease transaction - in some cases, it simply proved more reasonable for the parties (the equipment seller, buyer and leasing company) to apply a scheme where AS Starman was established as the seller of the goods in the leasing company.

Considering that, on the one hand, the company's creditworthiness has significantly improved and, on the other hand, the company still has interesting investment plans, the Starman's financing terms were reviewed together with the creditors in the second half of 2006. The best offer was made by the main financier SEB Ühisliising. On 22 September 2006, Starman concluded yet another sales and leaseback transaction, selling to SEB Ühisliising the cable network of Tallinn and its vicinity together with the signal origining Head-Ends locating at Akadeemia tee 28 for 8,667 thousand euros, and subsequently taking the sold non-current assets into finance lease for 7,030 thousand euros. The new lease contract was concluded for a term of 7 years, repayable in equal monthly instalments at an interest rate of 6-month Euribor + 1%. 6,737 thousand euros of the funds thus made available were used for premature termination of other previous finance lease contracts concluded with SEB Ühisliising. All respective collaterals related to terminated contracts were released, except for the 2nd-rank commercial pledge in the amount of 767 thousand euros, which was deemed non-material, and required additional administrative proceedings.

The finance lease balance of the new contract amounted to 6,811 thousand euros as of 31.12.2006. The remaining part of the finance lease balance as of 31.12.2006 has to do with finance lease used for financing the purchases of vehicles.

The group has acquired the following assets under finance lease (as of December 31, in thousands of euros):

	Land and buildings	Machinery and equipment	Total
2005			
Acquisition cost	7 544	5 240	12 784
Net book value	5 546	3 700	9 246
2006			
Acquisition cost	12 715	216	12 931
Net book value	9 269	141	9 409

The group has leased out, under operating lease, machinery and equipment with the following cost and net book value as of December 31 (in thousands of euros):

	2006	2005
Acquisition cost of assets leased out under operating lease[1]	2 440	1 408
Net book value of assets leased out under operating lease[1]	1 845	1 244
Revenue from operating lease	201	269

1 Among other things, the above assets include telephone modems which have been granted into the use of customers and which have an acquisition cost of 1,929 thousand euros and a net book value of 1,411 thousand euros in 2006 (1,173 thousand euros and 1,032 thousand euros in 2005, respectively).

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The company has acquired vehicles under operating lease terms (as of December 31, in thousands of euros):

	2006	2005
Operating lease payments in the period	49	56
Operating lease payments arising from non-rescindable contracts in future periods:	36	83
incl. payable within 1 year	25	50
1 - 5 years	11	33

Note 17 Related party transactions

For the purposes of this report, the following are considered related parties:

a. shareholders with significant influence and companies controlled by them;

b. management board and higher management, their close relatives and companies controlled by them.

The group has purchased services from the following related parties (in thousands of euros, per annum):

	2006	2005
Shareholders with significant influence	0	29
Companies related to members of the supervisory board	149	183

The company incurred the following liabilities from these transactions as of December 31 (recorded under accounts payable):

	2006	2005
Companies related to a member of the Supervisory Board	0	3

Services were sold to the members of the Management Board and the Supervisory Board and their relatives in the course of ordinary business. The total volume of the above services did not exceed 3 thousand euros in 2006 and 2005.

According to the Management Board of the company, the prices used for the above transactions do not differ from the market prices.

Management remuneration

A total of 280 thousand euros was paid in remuneration, with bonuses, to the members of the Management Board (in 2005: 251 thousand euros), and 21 thousand euros to members of the Supervisory Board (in 2005: 60 thousand euros).

Options have been issued to Management Board members under the bonus payment system approved by the company's Supervisory Board, allowing the Management Board members, under certain conditions, to acquire a total of 600,000 of the company's shares (see Note 20 and Note 15).

The members of Management Board have a right to termination benefits, provided that the member has not violated the Management Board member agreement. According to the contacts the maximum amount of such termination benefits is 63 thousand euros for all management members.

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Note 18 Note to the consolidated cash flow statement

in thousands of euros, per annum

Adjustments of net profit include the following gains/losses related to non-monetary operating activities, as well as revenue and expenses related to investing and financing activities:

	2006	2005
Depreciation, amortisation and impairments (Note 10, 11)	2 901	2 233
Gains from disposals of property, plant and equipment (Note 3)	-10	-15
Allowance for doubtful receivables	57	-24
Interest income	-21	-11
Interest expenses	326	285
Profit from change in fair value	0	-4
Income tax on dividends	87	0
Total adjustments of net profit	**3 340**	**2 465**

Purchase of non-current assets includes the following:

	2006	2005
Purchase of and additions to PPE (Note 10)	-4 962	-4 647
Purchase of and additions to intangible assets (Note 11)	-31	-16
PPE acquired under finance lease	148	485
Total acquisition of non-current assets	**-4 845**	**-4 178**

Note 19 Subsidiary company

On 20 September 2006, AS Starman and AS Levira founded Eesti Digitaaltelevisiooni AS, the principal activity of which is to supply digital terrestrial television services in Estonia. The services related to marketing and customer service are supplied to Eesti Digitaaltelevisiooni AS by AS Starman and the transmission service by AS Levira. The products are being sold under the ZUUM trademark held by Starman.

66% of shares in Eesti Digitaaltelevisiooni AS are held by Starman and 34% of the shares by Levira. According to the agreement, the shareholders will contribute pro rata with their shareholdings up to 3 million EUR to the company's equity. In the case of a need for additional financing the funds are to be provided by Starman and the shareholders would retain their current interest in profits and votes. The shareholders have signed an option agreement, according to which Levira is entitled and obliged to sell (has a put option) and Starman is entitled and obliged to acquire (has a call option) Levira's share on the agreed terms and conditions. The option can be exercised from 1 July 2008 depending primarily on the number of customers achieved. Most likely the option will be exercised when the number of customers reaches 35,000-50,000. Since Eesti Digitaaltelevisiooni AS is a starting company, it is impossible to reliably determine the value of the option agreement and, therefore, nothing related to that option is accounted in the financial statements.

As of 31 December 2006, the owners' contribution to the equity of Eesti Digitaaltelevisiooni AS amounted to 0.77 million EUR, of which the Group contributed 0.51 million euros. As of 31 December 2006, the loss of Eesti Digitaaltelevisiooni AS amounted to 156 thousand EUR, balance sheet total to 814 thousand EUR and owners' equity to 611 thousand EEK. The Group's share of the subsidiary's equity is 403 thousand euros. The subsidiaries shares are not listed on the stock exchange.

Note 20 Earnings per share

in thousands of euros

	2006	2005
Net profit attributable to shareholders (thousand EUR)	2 809	1 459
Weighted average number of shares (thousands of units)	13 054	13 054
Basic EPS (EEK)	**0,22**	**0,11**
Net profit attributable to shareholders (thousand EUR)	2 809	1 459
Weighted average number of shares (thousands of units)	13 054	13 054
Dilutive effect of options (thousands of units)*	9	0
Weighted average number of shares adjusted with options (thousands of units)	13 063	13 054
Diluted EPS (EEK)	**0,22**	**0,11**

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* The dilutive effect of options has been calculated as follows: 200,040 * (4.40 – 4.21) / 4.40 = 8,638 shares; incl. 200,040 = number of contingently issuable shares having dilutive effect, 4.40 = market value of shares as of 31.12.2006, 4.21 = share price upon exercise of option.

EPS (earnings per share) is calculated by dividing the net profit attributable to shareholders for the reporting period by the weighted average number of shares in the respective period.

The company has contingently issuable shares on account of options granted to management board members. The members of the management board are, subject to certain conditions, entitled to acquire a total of 600,000 shares in the company. The options have been divided into three series on the basis of the periods of realisation: the A series grants the right to acquire 200,040 shares from 1 July 2006 to 30 June 2008; the B series grants the right to acquire 199,980 shares from 1 July 2007 to 30 June 2009, and the C series grants the right to acquire 199,980 shares from 1 July 2008 to 30 June 2010. In the case of the A series, the option realisation price is equal to the average trade price applicable in the 3rd to the 8th week after the first day of trading in the shares on the stock exchange, plus 15%; for the B series the option realisation price is equal to the average trade price applicable during the 1st quarter of 2006, plus 15%, and for the C series the option realisation price is equal to the average trade price applicable during the 1st quarter of 2007, plus 15% (dividends paid will be deducted from the realisation price of options of all series). Several other conditions must be met for the options to be realised – specific criteria have been established for the company's financial results and market capitalisation as well as for the board member's employment relation with Starman.

Outstanding share options	2006	2005
Outstanding at the beginning of the period (thousands of units)	600	0
Granted during the period (thousands of units)	0	600
Outstanding at the end of the period (thousands of units)	600	600

As of the reporting date all conditions necessary for the realisation of the options of A-series had been met. Thus, the dilutive effect of underlying shares has been added to the weighted average number of shares during the period. Diluted EPS is calculated by dividing the net profit attributable to shareholders by the number of shares adjusted with dilutive effect of options.

Note 21 Pending disputes and legal actions

On 16 January 2006, AS Starman lodged a complaint with the Competition Board and the Communications Board by which it contested the plan of Elion Ettevõtted AS to raise, from 1 February 2006, rental charges payable for the use of communication ducts. The planned price increase for objects already leased out amounts to 32%. In the case of network expansion and renovation, planned price increase would be as much as 400%, plus subscription fee that has not been charged before. Starman's position is that the activity of Elion Ettevõtted AS is unlawful and incompatible with the Telecommunications Act, Competition Act and several other legal acts. Starman's expenses related to the rental of communication ducts amounted to nearly 0.5 million EUR in 2005. The actual enforcement of the proposed rental charges would have an immediate impact on the company in terms of the existing leased sites (potential increase of 32%), while any expansion or renovation of the network would in most cases prove to be economically unreasonable under such conditions. A prolonged continuation of such a situation might suppress the investing activities of the company. Expenses recorded for 2006 include the price increase proposed by Elion for the existing sites as from February. The company has carried out expansion or renovation of the cable network on the basis of the proposed new charges only where inevitable and to a very marginal extent.

On 7 April 2006, AS Starman filed a statement of claim with Harju County Court against AS Telset for recognition of the right of ownership and reclamation of things from illegal possession. The action to the value of 98 thousand EUR relates to the assets, which should have been included in the assets of AS Telset Telecommunications Group, a subsidiary acquired by Starman from Tele 2 OÜ in June 2004. The assets being reclaimed should have been transferred from AS Telset to Tele 2 Group when Tallinna Kaabeltelevisiooni AS, which was a subsidiary of Tele 2 Group at that time, acquired 100% of the shares in Telset Telecommunications Group. By its ruling of 10 April, the Harju County Court prohibited all transactions of AS Telset with these assets. During the first session held in October the court was unable to conduct a hearing on the merits; the next session was scheduled to take place in January 2007, but was postponed to the end of the next month. Expenses relating to the action have been insignificant so far, amounting to less than 3 thousand EUR.

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Note 22 Financial instruments

Credit risk

Credit risk stands for contingent damages caused to the company by the failure of its customers and business partners to fulfil their obligations. As of 31.12.2006 the company's maximum possible credit risk amounted to 1,043 thousand euros (31.12.2005: 694 thousand euros). This indicator is deeply theoretical, since due to the specifics of the company's operations (large number of customers with relatively small single payments), the company has no single material credit risks. In order to manage and minimise the overall credit risk, the company has established procedures for evaluating the solvency and for dealing with debtors. The company's available current assets are invested in highly creditworthy financial instruments.

Currency risk

The company is exposed to fluctuations in the US dollar exchange rate. Approximately 20% of the monthly expenses are directly or indirectly related to the fluctuations in the US dollar exchange rate. Similarly, investments in internet equipment and telephone modems are US dollar-based. Upon evaluating the currency risk on the background of the company's business activities, we find that the risk has a certain, although not important, effect on the results of operations. We must take into consideration, however, that, under the current market situation regarding the solutions offered, the company can only cover currency risks in a short perspective. As the USD exchange rate has risen to a sufficiently high level for the company, Starman concluded, in the end of November 2005, 26 forward transactions for the purchase of US dollars in the amount of 3,383 thousand USD, with terms of maturity of up to 10.11.2006. These transactions allowed to cover anticipated short USD positions 100% in the 6-month perspective and 50% in the 12-month perspective. As of 31.12.2005, the company had a total of 21 forward transactions in the total amount of 2,693 USD. The losses resulting from revaluation in the amount of 0.7 thousand euros are recorded as "Other payables" under "Payables" in the balance sheet. As it became obvious that the high US dollar exchange rate no longer bothered the company, with expectations of further weakening of the US dollar, Starman concluded, in May 2006, four forward transactions for sales of US dollars in the total amount of 600 thousand USD, thus reducing the cover for USD short positions in the second half of the year. As of 31.12.2006, the company had no more instruments designed for covering currency risks. For information on the effect of the concluded forward transactions on the financial results for 2006 - see the comment under "Other expenses" in Note 3. The company is expecting a further decrease in the share of operating expenses dependent on USD exchange rate fluctuations in 2007, partially because several contracts have been translated into euros. Since Starman currently does not expect the USD exchange rate to reach a level too high for a company in 2007, the short positions in USD will probably not be covered this year.

Interest rate risk

Most of the company's loan capital has been tied with the 6-month Euribor. The company is thus exposed to fluctuations in euro interest rates. Considering new, more favourable, financing terms agreed by the company in September 2006, interest expenses should not significantly increase in the near future even if euro interest rates are raised. By today, we can assume that most of the potential short-term rise in 6-month Euribor has already occurred by the beginning of 2007. The company monitors the changes in the international money market, and compares the financing offers with both floating and fixed interest rates. The effect of the interest rate risk on the results of the company's operations is very small. According to the management, there is no need for hedging these risks.

Fair value of assets and liabilities

According to the Management Board, the fair value of the Group's financial assets and liabilities does not materially differ from the net book value. The fair value of interest fund units is the market value of the units, and the fair value of cash (incl. deposits with term up to 3 months), bonds and other receivables/liabilities is calculated based on the discounted cash flow method.

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Note 23 Parent company's unconsolidated income statement

The financial information of the parent company (Notes 23-26) is comprised of separate principal reports of the parent company, disclosure of which is required by Estonian Accounting Law, even though this financial information is not a required part of the consolidated financial statements prepared under International Financial Reporting Standards as adopted by the European Union.

in thousands of euros, per annum

	2006	2005
Revenue	14 987	12 031
Other income	230	136
Goods, raw materials and services	-4 236	-3 869
Other operating expenses	-2 242	-2 076
Personnel expenses	-2 414	-2 024
Depreciation, amortisation and impairments	-2 901	-2 233
Other expenses	-133	-183
Operating profit	**3 292**	**1 783**
Net financial items	-293	-324
Profit before income tax	**2 999**	**1 459**
Income tax	-87	0
Net profit for the financial year	**2 912**	**1 459**

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Note 24 Parent company's unconsolidated balance sheet

in thousands of euros, as of December 31

	2006	2005
ASSETS		
Current assets		
Cash	717	282
Receivables	902	619
Prepayments	49	65
Inventories	992	760
Total current assets	**2 660**	**1 726**
Non-current assets		
Long-term financial investments	506	0
Other financial assets	0	10
Property, plant and equipment	18 982	17 210
Intangible assets	38	26
Total non-current assets	**19 526**	**17 246**
TOTAL ASSETS	**22 186**	**18 971**
LIABILITIES AND OWNER'S EQUITY		
Liabilities		
Current liabilities		
Borrowings	983	1 071
Payables	1 761	1 382
Prepayments	141	2 025
Total current liabilities	**2 885**	**2 582**
Non-current liabilities		
Long-term borrowings	6 211	5 997
Other long-term payables	280	203
Total non-current liabilities	**6 491**	**6 200**
Total liabilities	**9 376**	**8 782**
Owner's equity		
Share capital	8 343	8 343
Legal reserve	167	94
Retained earnings	4 301	1 753
Total owner's equity	**12 810**	**10 190**
TOTAL LIABILITIES AND OWNER'S EQUITY	**22 186**	**18 971**

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Note 25 Parent company's unconsolidated statement of changes in equity

in thousands of euros, per annum

	Share capital	Share premium	Legal reserve	Retained earnings	Total owner's equity
31.12.2004	**2 781**	**4 375**	**46**	**1 012**	**8 214**
Bonus issue	5 562	-4 375	0	-1 187	0
Transfers to legal reserve	0	0	48	-48	0
Profit for the financial year	0	0	0	1 459	1 459
Effect of merger with subsidiaries				517	517
31.12.2005	**8 343**	**0**	**94**	**1 753**	**10 190**
Announcement of dividends	0	0	0	-292	-292
Transfers to legal reserve	0	0	73	-73	0
Profit for the period	0	0	0	2 912	2 912
31.12.2006	**8 343**	**0**	**167**	**4 301**	**12 810**

Adjusted equity of the parent company which is a basis for a profit allocation according to the Estonian Accounting Law (as of December 31):

	2006	2005
Equity in the unconsolidated balance sheet of the parent company	12 810	10 190
Carrying value of the subsidiary in the unconsolidated balance sheet of the parent company	-506	0
Value of the subsidiary calculated in accordance with equity method accounting	403	0
Adjusted equity of the parent company	**12 707**	**10 190**

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Note 26 Parent company's unconsolidated cash flow statement

in thousands of euros, per annum

	2006	2005
Cash flow from operating activities		
Net profit	2 912	1 459
Adjustments of net profit	3 340	2 465
Merger of companies	0	144
Change in receivables and prepayments related to operating activities	-314	-38
Change in inventories	-210	-76
Change in liabilities and prepayments related to operating activities	468	260
Total cash flow from operating activities	**6 196**	**4 214**
Cash flow from investing activities		
Purchase of property, plant and equipment, and intangible assets	-4 729	-4 178
Proceeds from disposals of property, plant and equipment, and intangible assets	179	54
Investments into subsidiaries	-506	-415
Proceeds from disposals of other financial investments	0	209
Interest received	21	11
Total cash flow from investing activities	**-5 034**	**-4 320**
Cash flow from financing activities		
Loan repayments	-48	-48
Repayment of finance lease principal	-1 735	-1 195
Interest paid	-326	-285
Proceeds from sales and leaseback transactions	1 762	1 464
Dividends paid	-292	0
Paid income tax on dividends	-87	0
Total cash flow from financing activities	**-727**	**-64**
TOTAL CASH FLOW	**435**	**-169**
Cash and cash equivalents at the beginning of the period	282	451
Change in cash and cash equivalents	435	-169
Cash and cash equivalents at the end of the period	**717**	**282**

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02.04.2007

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Translation of the Estonian Original

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of AS Starman

Report on the Financial Statements

We have audited the consolidated financial statements of AS Starman and its subsidiaries (hereafter "the Group"), identified by us on the accompanying pages of the Consolidated Annual Report, which comprise the consolidated balance sheet as of December 31, 2006, the consolidated statements of income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards as adopted by the European Union. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as of December 31, 2006, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

Ernst & Young

Report on Other Legal and Regulatory Requirements

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The financial information of AS Starman as a parent company in Notes 23-26 is presented because it is required by the Estonian Accounting Law and is not a required part of the consolidated financial statements prepared under International Financial Reporting Standards as adopted by the European Union. Such financial information has been subject to the auditing procedures applied in our audit of the consolidated financial statements and, in our opinion, is prepared in all material respects in accordance with the requirements of the Estonian generally accepted accounting principles and in relation to the consolidated financial statements taken as whole.

Tallinn, April 2, 2007

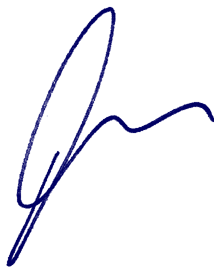
Hanno Lindpere
Ernst & Young Baltic AS

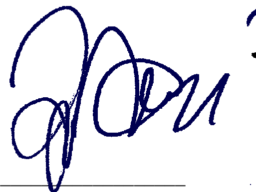
PROFIT ALLOCATION PROPOSAL

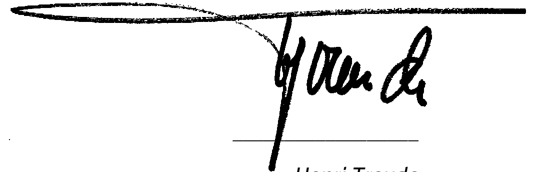
The Management Board proposes to the General Shareholders' Meeting of AS Starman to allocate the profit as follows:

Retained earnings as of 31.12.2006:	4 198 thousand euros
Transfer to legal reserve:	141 thousand euros
Net dividends to be paid:	584 thousand euros
Retained earnings after dividend payment:	3 473 thousand euros

0.70 EEK (approximately 0.045 EUR) per share is to be paid to shareholders in net dividends. Under the rules of the Tallinn Stock Exchange, the right to receive dividends shall be established on the basis of the list of security holders in the Estonian Central Register of Securities at 8:00 on the 10th stock exchange day after the General Shareholders' Meeting.



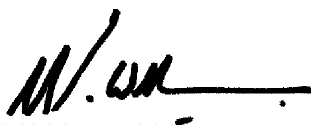




Peeter Kern	*Rändy Hütsi*	*Henri Treude*
Chairman of the Board	Member of the Board	Member of the Board

SIGNATURES OF THE MANAGEMENT BOARD AND SUPERVISORY BOARD TO THE ANNUAL REPORT 2006

We hereby confirm the correctness of the data presented in the consolidated Annual Report 2006:



Nigel Philip Williams

Chairman of the Supervisory Board

Roman Babka

Member of the Supervisory Board

Jaak Ennuste

Member of the Supervisory Board

Indrek Kuivallik

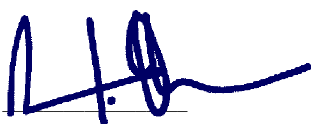
Member of the Supervisory Board

Hans Larsson

Member of the Supervisory Board

Rain Lõhmus

Member of the Supervisory Board

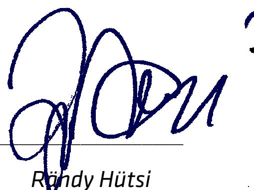


Sven Ilmar Oksaar

Member of the Supervisory Board

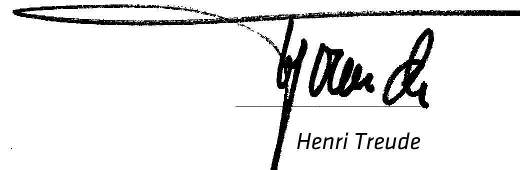
Peeter Kern

Chairman of the Management Board



Rändy Hütsi

Member of the Management Board



Henri Treude

Member of the Management Board