TALLINNA FARMAATSIATEHASE AS

Annual Report for
the Financial Year
Ended 31 December 2004

ANNUAL REPORT

Beginning of the financial year	1 January 2004
End of the financial year	31 December 2004
Name of the company	TALLINNA FARMAATSIATEHASE AS
Registration number	10093221
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Web-page	www.tft.ee
Field of activity	Production of pharmaceuticals
Auditors	AS Deloitte Audit Eesti
Documents enclosed with the annual report	Independent auditors' report Proposal for profit allocation

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General Data

The core activity of Tallinna Farmaatsiatehase AS is the production of pharmaceuticals. Tallinna Farmaatsiatehase AS is focusing mostly on the production of ointments since the second half of 2003.

As of 31 December 2004 the majority shareholder of Tallinna Farmaatsiatehase AS is PJSC Grindeks holding 93.519% of the share capital or 1 168 996 shares.

The number of employees as of 31 December 2004 was 71. The number of employees has declined by 21 or 23% compared with the end of 2003.

Management Board and Supervisory Council

In 2004 there were no changes in the Management Board or Supervisory Council.

Based on the decision by the Supervisory Council of Tallinna Farmaatsiatehase AS the Board has only one member since 19.03.2003 - Ibraim Muhtši as the Director.

Based on the decision of the shareholders of Tallinna Farmaatsiatehase AS the following Council members were elected from 25.07.2003:

Kirovs Lipmans	-	Chairman of the Council;
Vitalijs Gavrilovs	-	Member of the Council;
Valdis Jakobsons	-	Member of the Council.

Sales

The net sales of Tallinna Farmaatsiatehase AS in 2004 could be considered satisfactory. The sales of all finished goods were arranged as agreed between PJSC Grindeks and Tallinna Farmaatsiatehase AS on 21 July 2003. Subject to the agreement, the sales of the group's production have been arranged through the sales structures of Grindeks since financial year 2004. PJSC Grindeks is also responsible for the sales of the production of Tallinna Farmaatsiatehase AS in all markets.

In 2004 the sales of ointments increased by 13,576 thousand EEK or 28.6% compared with 2003. The most successful ointments continue to be Capsicam and Viprosal B, which are the original pharmaceuticals and trademarks developed by Tallinna Farmaatsiatehase AS.

Production and Product Development

On 1 July 2003 the Ministry of Social Affairs issued operating license No. 3667 to the Company until 1 July 2008 for the production of pharmaceuticals.

At the extraordinary shareholders' meetings on 25 July 2003 and 10 November 2003 the long-term strategy of the Company was approved, meaning that the Company concentrates on the production of ointments in the group.

In 2004 Tallinna Farmaatsiatehase AS produced over 10 different ointments. The output of the Company was approximately 8,5 million packages of ointments. Compared with 2003, the production of ointments increased by 16%. In 2004 the main products were Viprosal B and Capsicam ointments, accounting for 46% and 38% of the total ointment production, respectively.

In 2004 the Company continued the validation of the production procedures of ointment made by a new mixer.

Training continued to be a priority in 2004. The employees participated in the following courses: principles of management, financial reporting, production management and implementation according to GMP.

A lot of work has continuously been done to ensure that documentation complies with European Union requirements. In 2004, 10 pharmaceuticals were submitted for registration or re-registration in four countries. In 2004, 15 pharmaceuticals in 6 countries were registered. At the end of 2004 the Company had registered 131 pharmaceuticals in different markets. The number of registered pharmaceuticals at the end of 2003 was 134 showing the steady operations of the Company.

Financial Results

Comments to the Balance Sheet

As of 31 December 2004 the Company's total assets amounted to 61,874 thousand EEK, up by 5,034 thousand EEK or 8,9%.

The largest increase in assets has occurred in receivables from the parent of 16,083 thousand EEK or 157,9%. At the same time the inventories declined by 5,842 thousand EEK or 55,7%. Current assets in total increased by 6,959 thousand EEK or 28,1%.

Non-current assets declined from 32,071 thousand EEK at the beginning of 2004 to 30,146 thousand EEK at the end of 2004. Non-current assets accounted for 56,4% of total assets at the beginning of 2004 and 48,7% at the end of 2004. In 2004 the major investments were made for improvement of production equipment – purchasing and installation of water treatment equipment in ointment department and the external repairs of production unit premises.

At the end of 2004 long-term liabilities amounted to 536 thousand EEK. The current liabilities increased from 7,551 thousand EEK at the beginning of the year to 10,114 thousand EEK at the end of the year. At the same time the liquidity ratios of the Company improved. The Company's working capital (current assets – current liabilities) increased from 17,218 thousand EEK to 21,615 thousand EEK. The liquidity ratio (current assets – inventories / current liabilities) stood at 2.68 at the end of the year compared with 1.89 at the beginning of the year.

Equity increased in 2004 only by 3,107 thousand EEK, which is the amount of net profit for the financial year. Equity was up 6,5% to 51,224 thousand EEK. At the beginning of 2004 equity accounted for 84,7% of total assets compared with 82,8% at the end of 2004. The large percentage of equity is caused by very low level of liabilities.

Comments to the Income Statement

During 2004 the net sales amounted to 65,955 thousand EEK, down by 9,539 thousand EEK or 12,6% compared with 2003. Compared with 2003 the sales of ointments increased by 13,576 thousand EEK or 28,6%.

In 2004 other revenues amounted to 1,840 thousand EEK compared with 15,665 thousand EEK in 2003. In 2003 other revenues included the nonrecurring sale of intangible assets and royalties.

Materials, consumables and supplies dropped by 5,982 thousand EEK or 15,7% compared with 2003. Compared with 2003 miscellaneous operating expenses increased by 1,245 thousand EEK or 13,3% as a result of growing research and development costs (up by 1,223 thousand EEK). Personnel expenses dropped by 2,322 thousand EEK or 16,3%. Other expenses declined by 3,097 thousand EEK or 86,6%.

In 2004 operating profit declined by 7,485 thousand EEK or 70% compared with 2003. Net profit dropped by 7,122 thousand EEK. In 2004 the net profit amounted to 3,107 thousand EEK or 2,49 EEK per share.

Important events

The Director of Tallinna Farmaatsiatehase AS proposed to assemble the Extraordinary General Meeting of Shareholders on 8 September 2004. In the agenda was deciding on the takeover of shares belonging to minority shareholders by the majority shareholder. 93,46% of the votes represented by shares voted in favour of taking over the shares belonging to minority shareholders. Since the Commercial Code provides that the respective resolution shall be adopted if at least 95% of the votes represented by shares are in favour, the resolution was not adopted.

Future Outlook

The main goal for 2005 will be to ensure that the production would continuously meet the international requirements and standards. The main priority of Tallinna Farmaatsiatehase AS will be the production of ointments. The main task is the development of new ointments and their implementation to production.

Ibraim Muhtši
Director

DIRECTOR'S DECLARATION

The Director has prepared the annual accounts of Tallinna Farmaatsiatehase AS for the financial year ended 31 December 2004.

The annual accounts have been prepared according to the International Financial Reporting Standards (IFRS), and present a true and fair view of the financial position, economic performance and cash flows of Tallinna Farmaatsiatehase AS.

Preparation of the annual accounts according to IFRS involves estimates made by the Director on Tallinna Farmaatsiatehase AS assets and liabilities as of the balance sheet date, and on income and expenses during the financial year. These estimates are based on up-to-date information about the state of Tallinna Farmaatsiatehase AS and consider the plans and risks as of the date of the annual accounts' preparation. The actual outcome of the business transactions recorded may differ from those estimates.

Significant circumstances that have an effect on the valuation of assets and liabilities until the preparation of the annual accounts on 10 March 2005 are taken into consideration.

The Director considers Tallinna Farmaatsiatehase AS to carry its activities as a going concern.

Name	Position	Signature	Date
Ibraim Muhtši	Director		31.03.05.

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BALANCE SHEETS
AS OF 31 DECEMBER 2004 AND 2003

ASSETS	Note	31.12.2004 EEK	31.12.2003 EEK
Current assets			
Cash and bank accounts	2	308 230	1 268 124
Trade and other current receivables	3	26 766 362	13 004 988
Inventories	4	4 653 850	10 495 893
Total current assets		**31 728 442**	**24 769 005**
Non-current assets			
Other long-term receivables	5	104 573	344 110
Fixed assets	6	29 648 870	31 171 826
Intangible assets	7	392 124	555 076
Total non-current assets		**30 145 567**	**32 071 012**
TOTAL ASSETS		**61 874 009**	**56 840 017**

LIABILITIES AND EQUITY	Note	31.12.2004 EEK	31.12.2003 EEK
Current liabilities			
Short-term debt obligations	8	767 529	740 846
Trade and other current payables	9	9 346 252	6 810 569
Total current liabilities		**10 113 781**	**7 551 415**
Non-current liabilities			
Long-term debt obligations	8	536 440	1 171 335
Total non-current liabilities		**536 440**	**1 171 335**
Total liabilities		**10 650 221**	**8 722 750**
Equity			
Share capital	10	12 500 000	12 500 000
Reserves	11	2 316 210	2 316 210
Retained earnings		33 301 057	23 073 031
Net profit for the financial year		3 106 521	10 228 026
Total equity		**51 223 788**	**48 117 267**
TOTAL LIABILITIES AND EQUITY		**61 874 009**	**56 840 017**

The notes presented on pages 11 to 25 form an integral part of the annual accounts.

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INCOME STATEMENTS
FOR THE FINANCIAL YEARS 2004 AND 2003

	Note	2004 EEK	2003 EEK
Net sales	12	65 955 001	75 493 863
Other income	13	1 839 890	15 664 587
Change in inventories of finished goods and work-in-progress		(5 614 810)	(7 410 435)
Materials, consumables and supplies	14	(32 211 917)	(38 193 980)
Miscellaneous operating expenses	15	(10 632 646)	(9 387 641)
Personnel expenses	16	(11 925 515)	(14 247 938)
Depreciation, amortisation and value adjustments	6, 7	(3 723 138)	(7 649 055)
Other expenses		(478 707)	(3 575 863)
Operating profit		**3 208 158**	**10 693 538**
Financial income and expenses	17	(101 637)	(465 512)
Net profit for the financial year		**3 106 521**	**10 228 026**
Earnings per share	18	**2.49**	**8.18**

The notes presented on pages 11 to 25 form an integral part of the annual accounts.

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STATEMENTS OF CHANGES IN EQUITY FOR THE FINANCIAL YEARS 2004 AND 2003

	Share capital EEK	Reserves EEK	Retained earnings EEK	Net profit for the financial year EEK	Total EEK
31 December 2002	**12 500 000**	**2 316 210**	**18 077 916**	**4 995 115**	**37 889 241**
Allocation of net profit for the financial year to retained earnings	-	-	4 995 115	(4 995 115)	-
Net profit for the financial year	-	-	-	10 228 026	**10 228 026**
31 December 2003	**12 500 000**	**2 316 210**	**23 073 031**	**10 228 026**	**48 117 267**
Allocation of net profit for the financial year to retained earnings	-	-	10 228 026	(10 228 026)	-
Net profit for the financial year	-	-	-	3 106 521	**3 106 521**
31 December 2004	**12 500 000**	**2 316 210**	**33 301 057**	**3 106 521**	**51 223 788**

Additional information for share capital is provided in note 10 and for reserves in note 11 to the annual accounts.

The notes presented on pages 11 to 25 form an integral part of the annual accounts.

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CASH FLOW STATEMENTS
FOR THE FINANCIAL YEARS 2004 AND 2003

	Note	2004 EEK	2003 EEK
OPERATING ACTIVITIES			
Net profit for the financial year		3 106 521	10 228 026
Transformation of net profit from operating activities into net cash flows:			
Depreciation and amortisation	6, 7	3 723 138	7 649 055
Gain from disposal of fixed assets	13	(17 086)	(249 562)
Gain from disposal of intangible assets	13	-	(11 850 594)
Loss from write-off of prepayments for intangible assets		342	576 103
Write-off of loan	5	237 410	-
Interest income	17	(10 534)	(24 202)
Interest expense	17	125 393	1 907 282
Changes in current assets and current liabilities:			
Trade and other current receivables		(13 783 581)	10 636 818
Inventories		5 842 043	9 569 559
Trade and other current payables		2 535 683	(2 728 421)
Cash flows from operating activities		**1 759 329**	**25 714 064**
INVESTING ACTIVITIES			
Acquisition of fixed assets	6, 7	(1 733 436)	(2 933 808)
Proceeds from disposal of fixed assets		21 000	249 562
Repayments of loans granted		22 548	28 795
Interest received		12 320	25 737
Cash flows used in investing activities		**(1 677 568)**	**(2 629 714)**
FINANCING ACTIVITIES			
Repayments of loans raised		-	(18 829 748)
Repayments of finance lease		(916 262)	(1 098 047)
Interest paid		(125 393)	(1 966 095)
Cash flows used in financing activities		**(1 041 655)**	**(21 893 890)**
Change in cash		**(959 894)**	**1 190 460**
CASH AT THE BEGINNING OF THE YEAR		**1 268 124**	**77 664**
CASH AT THE END OF THE YEAR		**308 230**	**1 268 124**

The notes presented on pages 11 to 25 form an integral part of the annual accounts.

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NOTE 1. ACCOUNTING POLICIES

The annual accounts of Tallinna Farmaatsiatehase AS (hereinafter also "the Company") have been prepared in accordance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB).

The annual accounts have been prepared in Estonian kroons (EEK).

The annual accounts are prepared on the historical cost basis if not indicated differently in the accounting policies as set out below.

Foreign currency transactions

Foreign currency transactions are recorded at the foreign currency exchange rates quoted by the Bank of Estonia at the transaction date. Monetary and non-monetary assets and liabilities, denominated in foreign currencies, which are recorded at fair value, are translated into EEK using the official foreign currency exchange rates valid on the balance sheet date. Gains and losses from foreign currency transactions are recorded as net in the income statement. The following are the applicable rates of the principal currencies in EEK:

Currency	31.12.2004	31.12.2003
USD	11,4711	12,4096
EUR	15,6466	15,6466

Financial assets and liabilities

Cash, trade receivables, accrued income, other short and long-term receivables are considered to be financial assets. Trade payables, accrued expenses, other short and long-term payables are considered to be financial liabilities.

Financial assets and liabilities are initially measured at cost, which is the fair value of consideration given or received to acquire the financial asset or liability. Transaction costs are included in the initial measurement of all financial assets and liabilities.

Financial assets and liabilities are recognised on the balance sheet, when the title is transferred to in accordance with the contract terms.

Cash and bank accounts

Cash and bank accounts comprise cash on hand and demand bank deposits.

Cash flows from operating activities are prepared using the indirect method. Cash flows from investing and financing activities are reported based on gross receipts and disbursements made during the accounting period.

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Valuation of receivables

Receivables recorded on the balance sheet are valued on the basis of the estimated recoverable amount. Accounts receivable considered to be doubtful are expensed during the financial year. Receivables, which were expensed, but then collected during the financial year, are recorded on the same expense account as a reverse entry.

Inventories

Purchased goods, raw materials and supplies are recorded at cost, which comprises direct and indirect acquisition expenditures incurred without which the inventories would not be in their present condition and quantity. Finished goods and work-in-progress are recorded at production cost, which consists of direct and indirect manufacturing costs.

Inventories are expensed applying the weighted average method. Inventories are stated on the balance sheet at the lower of cost and net realisable value.

Fixed assets

Fixed assets with a useful life of over one year and with a minimum value of 5 000 EEK are considered to be fixed assets. Fixed assets are recorded at cost, which comprises purchase price, non-refundable taxes and other directly attributable expenditures.

Depreciation is charged using the straight-line method. Depreciation rates are set separately to each fixed asset depending on its estimated useful life as follows:

- buildings – 4% per annum;
- machinery and equipment – 10-25% per annum;
- other equipment – 25% per annum.

The improvements to fixed assets are capitalized if the asset is improved to a qualitatively new level, or if it is possible to prove that the revenue resulting from the expenditure made will be generated during the future periods. Maintenance and repairs are expensed.

Intangible assets

The sales and production licenses of pharmaceuticals are recorded as intangible assets. Licenses are recorded at cost and amortised on a straight-line basis over their validity period. All recorded licenses are valid up to five years. Amortisation is recognised as a decrease of net book value on the balance sheet and expensed in the income statement as "Depreciation, amortisation and value adjustments".

Impairment of assets

At each balance sheet date, a review of whether there is any indication that assets have suffered an impairment loss, is performed. If the management of the Company detects any indications that the value of an asset may have declined below its carrying amount, the recoverable amount of the asset is estimated. Where it is not possible to estimate the recoverable amount of an individual asset, the recoverable amount is estimated for the cash-generating unit to which the asset belongs.

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The recoverable amount is the greater of the net selling price and value in use. In assessing value in use, the estimated future cash flows from continuous use and subsequent disposal are discounted to their present value using a discount rate that reflects expected return on similar investments.

If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. An impairment loss is recognized as an expense as "Depreciation, amortisation and value adjustments".

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount. The increased carrying amount does not exceed the carrying amount that would have been determined, if no impairment loss had been recognized for the asset in prior years.

Leases

Leases are classified as finance leases whenever the term of the lease transfer substantially all the risks and rewards of ownership to the lessee. Other leases are classified as operating leases.

The Company as lessee

Finance leases are recognised on the balance sheet by recording an asset and a liability equal to the present value of minimum lease payments at the inception of the lease. Leased fixed assets are depreciated in accordance with the principles described above. The maximum period of depreciation is the estimated useful life of the asset. Repayments of the principal reduce lease liabilities, whilst the finance charge component of the lease payment is charged directly to expense.

Rentals payable under operating leases are charged to the income statement on a straight-line basis over the term of the relevant lease, irrespective of disbursements for relevant payables. The asset leased under operating lease is not recorded on the balance sheet.

Research and development costs

Research and development costs are charged as miscellaneous operating expenses for the period during which they incurred.

Liabilities

Liabilities with payment terms over one year from the balance sheet date are considered to be long-term liabilities. Other liabilities are reported as short-term.

Potential liabilities, guarantees and warranties are disclosed in the notes to the annual accounts as contingent liabilities.

Taxation

The Income Tax Law that became effective in Estonia on 1 January 2000 replaces the taxation of earnings with the taxation of dividend distributions and other payments that have the characteristics of profit distribution. Due to the principles of taxation, the term *tax base of assets and liabilities* does not have substance and deferred income tax assets and liabilities as defined in IAS 12 (Income Taxes) cannot arise.

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Revenue recognition

Net sales are recorded on the accrual basis of accounting, when the significant risks related to ownership of goods have been transferred to the buyer and the costs incurred in respect of the transaction can be measured reliably. Net sales comprise the revenue earned from goods and services sold from which discounts and returned goods have been subtracted. Net sales from services are recorded in the period when the service has been provided.

Interest income is recorded on the accrual basis of accounting.

Segment reporting

The Company operates in the field of ointment production in Estonia. Finished goods are fully sold to the Company's parent PJSC Grindeks in Latvia. As a result of the reasons mentioned above the Company's operations are handled as in one business and geographical segment.

Earnings per share

Basic earning per chare is calculated by dividing the net profit of the period by the weighted average number of ordinary shares. The Company has no potential ordinary shares and therefore basic earnings per share and diluted earnings per share are equal.

Subsequent events

Significant circumstances, occurring during the preparation period of the annual accounts and that are related to the transactions which took place during the financial year or previous periods and confirm the conditions that existed at the balance sheet date, are considered in the valuation of assets and liabilities.

Significant events, occurring during the preparation period of the annual accounts which are not considered in the valuation of assets and liabilities but which significantly influence the results of the next financial year, are disclosed in the notes to the annual accounts.

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NOTE 2. CASH AND BANK ACCOUNTS

	31.12.2004 EEK	31.12.2003 EEK
Cash on hand	4 604	4 172
Bank accounts in EEK	16 970	786 445
Bank accounts in foreign currency	281 277	472 111
Other cash equivalents	5 379	5 396
Total	**308 230**	**1 268 124**

NOTE 3. TRADE AND OTHER CURRENT RECEIVABLES

	31.12.2004 EEK	31.12.2003 EEK
Trade receivables	16 258	2 250 283
Receivables from parent and other group companies (see note 19)	26 311 414	10 188 177
Other short-term receivables	38 801	76 574
Accrued income	-	1 786
Prepaid taxes	354 418	433 108
Other prepaid expenses	45 471	55 060
Total	**26 766 362**	**13 004 988**

NOTE 4. INVENTORIES

	31.12.2004 EEK	31.12.2003 EEK
Raw material	2 321 703	2 428 072
Work-in-progress	108 177	-
Finished goods		
In Estonian plant	1 010 851	2 532 952
In consignment warehouses	-	4 978 068
In quality control	1 213 119	435 937
Total finished goods	2 223 970	7 946 957
Prepayments to suppliers	-	120 864
Total	**4 653 850**	**10 495 893**

In 2004 and 2003 the materials unsuitable for production and realisation were recognised as impaired in the amount of 77 788 EEK and 420 678 EEK, respectively.

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NOTE 5. OTHER LONG-TERM RECEIVABLES

The Company has granted the following loans:

	31.12.2004 EEK	31.12.2003 EEK
Long-term unsecured loans to private persons with annual interest rate of 5,7%, contract currency EEK, maturity date January 2018.	135 366	395 324
Including short-term portion	30 793	51 214
Long-term portion	**104 573**	**344 110**

As of 31 December 2004 a long-term loan has been granted to the Director, Ibraim Muhtši, in the amount of 104 573 EEK. In 2004, the Supervisory Council decided to waive the loan granted to the Director in the amount of 237 410 EEK. The short-term portion of loans granted in the amount of 30 793 EEK is recorded as "Trade and other current receivables".

The repayments of granted loans presented above are as follows:

	EEK
Within 1 year	30 793
1-5 years	27 062
After 5 years	77 511
Total	**135 366**

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NOTE 6. FIXED ASSETS

The statement of fixed assets is as follows:

	Land and buildings EEK	Machinery and equipment EEK	Other fixed assets EEK	Construction-in-progress EEK	Prepay-ments for fixed assets EEK	Total EEK
Acquisition cost						
31 December 2003	**31 554 379**	**14 921 278**	**2 980 626**	**-**	**2 155 100**	**51 611 383**
Additions	29 300	450 672	26 949	806 267	669 688	**1 982 876**
Disposals	-	(255 000)	(19 055)	-	-	**(274 055)**
Reclassification	2 420 616	1 210 439	-	(806 267)	(2 824 788)	**-**
31 December 2004	**34 004 295**	**16 327 389**	**2 988 520**	**-**	**-**	**53 320 204**
Accumulated depreciation						
31 December 2003	**9 402 856**	**8 518 735**	**2 517 966**	**-**	**-**	**20 439 557**
Depreciation	1 473 878	1 854 312	173 728	-	-	**3 501 918**
Disposals	-	(255 000)	(15 141)	-	-	**(270 141)**
31 December 2004	**10 876 734**	**10 118 047**	**2 676 553**	**-**	**-**	**23 671 334**
Carrying amount						
31 December 2003	**22 151 523**	**6 402 543**	**462 660**	**-**	**2 155 100**	**31 171 826**
31 December 2004	**23 127 561**	**6 209 342**	**311 967**	**-**	**-**	**29 648 870**

As of 31 December 2004 and 2003 the carrying amount of fixed assets acquired through finance lease amounted to 2 385 601 EEK and 2 935 215 EEK, respectively. In 2004, the acquisition cost of assets acquired through finance lease, amounted to 308 050 EEK.

As a result of the reorganisation of production the balance sheet of the Company includes idle buildings and facilities in the carrying amount of 3 096 185 EEK. According to the valuation of an independent expert the fair value of these assets is higher than their carrying amount.

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NOTE 7. INTANGIBLE ASSETS

The statement of intangible assets is as follows:

	Patents and licenses EEK	Prepay-ments for intangible assets EEK	Total EEK
Acquisition cost			
31 December 2003	**1 349 730**	**16 442**	**1 366 172**
Additions	-	58 610	**58 610**
Reclassification	16 100	(16 100)	-
Disposals	-	(342)	**(342)**
31 December 2004	**1 365 830**	**58 610**	**1 424 440**
Accumulated amortisation			
31 December 2003	**811 096**	-	**811 096**
Amortisation	221 220	-	**221 220**
31 December 2004	**1 032 316**	-	**1 032 316**
Carrying amount			
31 December 2003	**538 634**	**16 442**	**555 076**
31 December 2004	**333 514**	**58 610**	**392 124**

The licenses for sale of pharmaceuticals are recorded as intangible assets. The pharmaceuticals are registered for five years and are amortised respectively. Expenses on registration of pharmaceuticals amounted to 524 445 EEK and 893 555 EEK, in 2004 and 2003, respectively.

The Company continues to register the tablet pharmaceuticals until their re-registration to the name of PJSC Grindeks (latest within 24 months).

In 2004, the following pharmaceuticals were registered in different countries:

Estonia	Viprosal B ointment
Latvia	Digoxin TFT tbl, Ibuprofen 200 TFT tbl, Paracetomol 500 TFT tbl, Piracetam TFT capsules, Piroxicam TFT tbl
Belarus	Apilak tbl, Digoxin tbl, Piroxicam tbl, Viprosal B ointment
Georgia	Piroxicam tbl, Cyclodol tbl, Digoxin tbl
Armenia	Cyclodol tbl
Hungary	Viprosal B ointment

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As of 31.12.2004 and 31.12.2003, the following number of pharmaceuticals has been registered in different countries:

	31.12.2004	31.12.2003
Belarus	23	28
Estonia	19	27
Georgia	17	16
Latvia	14	9
Russia	13	13
Kazakhstan	13	13
Ukraine	9	9
Moldova	9	9
Armenia	7	5
Lithuania	5	3
Poland	1	1
Hungary	1	1

NOTE 8. LEASES

Finance lease – the Company as lessee

The Company has the following liabilities on financing the acquisition of production equipment:

	31.12.2004 EEK	31.12.2003 EEK
Long-term finance lease liability to Ühisliisingu AS with annual interest rate 5.6%, maturity date July 2006, contract currency EEK. The liability is secured by asset.	1 171 335	1 821 427
Long-term finance lease liability to Hansa Liising Eesti AS with annual interest rate 4.9%, maturity date July 2007, contract currency EUR. The liability is secured by asset.	132 634	-
Long-term finance lease liability to AS Nordea Finance Estonia with annual interest rate 8%, maturity date September 2004, contract currency EUR. The liability is secured by asset.	-	90 754
Total	**1 303 969**	**1 912 181**
Including short-term portion	767 529	740 846
Long-term portion	**536 440**	**1 171 335**

The repayments of the liabilities presented above are as follows:

	EEK
Within 1 year	767 529
1-5 years	536 440
Total	**1 303 969**

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Operating lease – the Company as lessee

The Company leases 11 cars and one truck with the minimum operating lease obligations as follows:

	EEK
Within 1 year	316 036
1-5 years	354 495
Total	**670 531**

The Company's operating lease expenses in 2004 and 2003 were 313 091 EEK and 452 393 EEK, respectively.

Staring from 8 July 2004 the Company has subleased five cars to PAS Grindeks Estonian branch subject to the agreement with Hansa Liising Eesti AS.

NOTE 9. TRADE AND OTHER CURRENT PAYABLES

	31.12.2004 EEK	31.12.2003 EEK
Accounts payable	7 317 255	4 839 076
Taxes payable	417 866	-
Accrued expenses	1 164 317	1 524 679
Dividends payable	446 814	446 814
Total	**9 346 252**	**6 810 569**

Dividends payable consists of unpaid dividends to the state from the net profit of 1994.

NOTE 10. SHARE CAPITAL

As of 31.12.2004 and 31.12.2003 the share capital of the Company is 12 500 000 EEK consisting of 1 250 000 shares with a nominal value of 10 EEK. The shares have been fully paid for. The shares of the Company are listed in the secondary list of Tallinn Stock Exchange.

As of 31.12.2004 and 31.12.2003 the shareholders of the Company are the following:

	31.12.2004	31.12.2003
PJSC Grindeks	93,5%	64,1%
Hansabanka Clients	-	22,5%
incl. PJSC Grindeks	-	*10,5%*
Norberg Capital Group Inc	-	1,1%
Other minority shareholders	6,5%	12,3%
Total	**100,0%**	**100,0%**

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NOTE 11. RESERVES

Statutory legal reserve of 1 250 000 EEK has been established in accordance with the requirements of the Commercial Code. Every year, companies have to transfer to statutory legal reserve at least 1/20 of their net profit until the reserve amounts to 1/10 of share capital. Statutory legal reserve may be used to cover losses and to increase share capital. Statutory legal reserve cannot be used to make distributions to the shareholders.

Other reserve of 1 066 210 EEK was allocated from the net profit of 1995 to the going concern reserve. The management has not determined the use of other reserve.

NOTE 12. NET SALES

Net sales are divided by markets as follows:

	2004 EEK	%	2003 EEK	%
Latvia	65 809 437	100	57 567 038	76
Estonia	145 564	-	17 926 825	24
Total	**65 955 001**	**100**	**75 493 863**	**100**

Starting from 2004, all production of the Company is sold through the parent PJSC Grindeks.

Net sales are divided by product groups as follows:

	2004 EEK	%	2003 EEK	%
Ointments	61 103 736	93	47 527 934	63
Injections	1 717 442	3	12 302 709	16
Tablets	992 173	1	5 777 444	8
Other	2 141 650	3	9 885 776	13
Total	**65 955 001**	**100**	**75 493 863**	**100**

NOTE 13. OTHER INCOME

	2004 EEK	2003 EEK
Foreign exchange gain	314 753	-
Gain on disposal of intangible assets	-	11 850 594
Royalty	-	3 440 223
Gain on disposal of fixed assets	17 086	249 562
Other revenue	1 508 051	124 208
Total	**1 839 890**	**15 664 587**

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NOTE 14. MATERIALS, CONSUMABLES AND SUPPLIES

	2004 EEK	2003 EEK
Raw materials	(29 439 548)	(29 479 139)
Energy	(1 383 145)	(1 557 159)
Registration of pharmaceuticals, trademarks	(653 512)	(1 066 292)
Transportation of finished goods	(498 390)	(532 858)
Goods	(34 775)	(5 279 383)
Fuel and other cost of materials	(202 547)	(279 149)
Total	**(32 211 917)**	**(38 193 980)**

NOTE 15. MISCELLANEOUS OPERATING EXPENSES

	2004 EEK	2003 EEK
Training and consultations	(4 059 643)	(2 273 217)
Outsourced services	(1 623 650)	(2 006 182)
Research and development costs	(1 851 022)	(628 150)
Repairs	(692 257)	(692 038)
Leasing, rent	(335 842)	(466 292)
Sales and marketing expenses	(612 300)	(1 460 206)
Miscellaneous fees	(269 138)	(465 613)
Transport	(243 561)	(395 722)
Business trips	(132 212)	(109 211)
Office expenses	(94 101)	(134 362)
Representation costs	(88 837)	(266 482)
Other expenses	(630 083)	(490 166)
Total	**(10 632 646)**	**(9 387 641)**

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NOTE 16. PERSONNEL EXPENSES

	Salary		Average number of employees	
	2004 EEK	2003 EEK	2004	2003
Salaries and wages	**(8 920 390)**	**(10 562 226)**	**83**	**113**
incl. workers	(1 777 691)	(2 408 479)	40	60
administration	(5 555 558)	(6 229 406)	42	52
board	(570 673)	(825 000)	1	1
other personnel expenses	(1 016 468)	(1 099 341)	-	-
Social taxes	**(3 005 125)**	**(3 685 712)**	-	-
Total	**(11 925 515)**	**(14 247 938)**	**83**	**113**

In 2004, the average number of employees in the Company was 83, of whom 42 were specialists or managers. The average salary in 2004 was 7 936 EEK per month. In 2003, the average number of employees was 113, of whom 52 were specialists or managers. The average salary in 2003 was 6 979 EEK per month.

NOTE 17. FINANCIAL INCOME AND EXPENSES

	2004 EEK	2003 EEK
Interest expenses	(125 393)	(1 907 282)
Foreign exchange gain	13 222	1 472 684
Other financial income and expenses	10 534	(30 914)
Total	**(101 637)**	**(465 512)**

NOTE 18. EARNINGS PER SHARE

	2004 EEK	2003 EEK
Net profit for the financial year	3 106 521	10 228 026
Weighted average number of shares	1 250 000	1 250 000
Earnings per share (EPS)	**2.49**	**8.18**

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NOTE 19. RELATED PARTY TRANSACTIONS

The transactions with related parties are transactions with the parent PJSC Grindeks, its Estonian branch, director, members of the management and the Supervisory Council, their relatives and the companies under their control.

The transactions with related parties in 2004 and 2003 are the following:

	2004 EEK	2003 EEK
Net sales		
PJSC Grindeks	65 809 437	57 567 038
Other revenues		
PJSC Grindeks	126 765	-
PAS Grindeks Estonian branch	49 011	-
Total	**175 776**	**-**
Materials, consumables and supplies		
PJSC Grindeks	260 294	5 221 463
Miscellaneous operating expenses		
PJSC Grindeks	180 852	409 965
Interest expenses		
PJSC Grindeks	-	923 205

Prices used in transactions with related parties are agreed prices.

Balances with related parties are the following:

	31.12.2004 EEK	31.12.2003 EEK
Accounts receivable		
PJSC Grindeks	26 270 926	10 188 177
PAS Grindeks Estonian branch	40 488	-
Total	**26 311 414**	**10 188 177**

In 2004 salaries and wages paid to the Director and members of the Supervisory Council amounted to 570 673 EEK and 324 000 EEK, respectively.

Potential liability arising from termination of employment contracts with the members of the management amounts to 199 500 EEK, including taxes.

The Company has also granted a loan to the Director (see note 5).

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NOTE 20. FINANCIAL RISKS

Currency risk

Export accounts for 100% of the Company's net sales. Since 2004 the export invoices are issued in EUR (USD in 2003). The Company does not use currency options and forward contracts.

Foreign currency positions as of 31.12.2004 were as follows:

	Assets EEK	Liabilities EEK	Net position EEK
USD	-	(191 772)	(191 772)
EUR	26 270 926	(3 413 920)	22 857 006
Total	**26 270 926**	**(3 605 692)**	**22 665 234**

Credit risk

Accounts receivable from the parent are 99% of total receivables. Credit risk is directly related to the solvency of the parent company.

Interest risk

The activities of the Company are financed with equity instruments. External financing (finance lease) has been used for the purchase of machinery and equipment. The contract currency of leasing agreement is EEK or EUR and interest rates are fixed for the whole lease term.

Since the share of external financing in the total capital structure is insignificant, the related risks are minimal.

Fair value

The management believes that the fair values of the Company's financial assets and liabilities as of 31.12.2004 do not differ materially from their carrying amounts.

NOTE 21. POTENTIAL INCOME TAX ON DIVIDENDS

According to the Estonian Income Tax Act the accrued profit of a resident legal entity is not subject to corporate income tax, instead the tax is due on the dividend distribution. Resident legal entities are, since 1 January 2003, liable to income tax on all dividends paid and other profit distributions irrespective of the recipient (Income Tax Act, section 50). The tax rate applicable is 24/76 on the dividends paid.

The contingent tax liability that may occur if all distributable retained earnings should be paid out as dividends is not reported on the balance sheet. The income tax due on dividend distribution is expensed in the income statement when dividends are declared.

The Company's retained earnings that may be distributed as of 31 December 2004 amounted to 36 407 578 EEK. Consequently, the maximum possible tax liability which would become payable if retained earnings were fully distributed is 11 497 130 EEK.

* * *

DIRECTOR'S AND SUPERVISORY COUNCIL'S SIGNATURES TO THE ANNUAL REPORT FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2004

The Director has prepared the management report and the annual accounts of Tallinna Farmaatsiatehase AS on 10 March 2005.

The Supervisory Council of Tallinna Farmaatsiatehase AS has reviewed the annual report, prepared by the Director, consisting of the management report and the annual accounts, Director's proposal for profit allocation and the independent auditors' report, and approved the annual report for presentation on the Shareholders' General Meeting.

The annual report has been signed by the Director and all the members of the Supervisory Council.

Name	Position	Signature	Date
Ibraim Muhtši	Director		31.03.05
Kirovs Lipmans	Chairman of the Council		31.03.05
Vitalijs Gavrilovs	Member of the Council		31.03.05
Valdis Jakobsons	Member of the Council		31.03.05

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[Translation from Estonian]

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Tallinna Farmaatsiatehase AS:

We have audited the annual accounts of Tallinna Farmaatsiatehase AS ("the Company") for the year ended 31 December 2004. These annual accounts are the responsibility of the Company's Director. Our responsibility is to express an opinion on these annual accounts based on our audit.

We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the annual accounts are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the annual accounts. An audit also includes assessing the accounting principles used and significant estimates made by the management, as well as evaluating the overall presentation of the annual accounts. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the annual accounts present fairly, in all material respects, the financial position of the Company as of 31 December 2004, the results of its operations and its cash flows for the year then ended, in accordance with Estonian Accounting Law and International Financial Reporting Standards.

Toomas Prükk
Certified Auditor
31 March 2005

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PROPOSAL FOR PROFIT ALLOCATION

The Director of Tallinna Farmaatsiatehase AS proposes to allocate the net profit for 2004 in the amount of 3 106 521 EEK to retained earnings.

10 March 2005

Ibraim Muhtši
Director