



Arco Vara AS

Interim report II quarter 2011



ARCO REAL ESTATE

INTERIM REPORT
SECOND QUARTER AND SIX MONTHS
ENDED 30 JUNE 2011
(UNAUDITED)

Company name: Arco Vara AS

Registry number: 10261718

Address: Jõe 2b, 10151 Tallinn, Republic of Estonia

Telephone: +372 6 144 630

Fax: +372 6 144 631

E-mail: info@arcovara.ee

Corporate website: www.arcorealestate.com

Core activities: Construction of buildings (EMTAK 41000)
Civil engineering (EMTAK 42000)
Specialised construction activities (EMTAK 43000)
Real estate activities (EMTAK 6800)

Financial year: 1 January 2011 – 31 December 2011

Reporting period: 1 January 2011 – 30 June 2011

Supervisory board: Richard Tomingas, Hillar-Peeter Luitsalu, Ragnar Meitern,
Kalev Tanner, Aare Tark

Management board: Lembit Tampere

Auditor: KPMG Baltics OÜ

CONTENTS

DIRECTORS' REPORT	4
GROUP CHIEF EXECUTIVE'S REVIEW	8
CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS	17
CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME	17
CONSOLIDATED STATEMENT OF FINANCIAL POSITION	18
CONSOLIDATED STATEMENT OF CASH FLOWS	19
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY	20
NOTES TO THE CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS	21
1. SIGNIFICANT ACCOUNTING POLICIES	21
2. SEGMENT REPORTING BY BUSINESS SEGMENTS	21
3. COST OF SALES.....	22
4. DISTRIBUTION EXPENSES	22
5. ADMINISTRATIVE EXPENSES	22
6. FINANCE INCOME AND EXPENSES	23
7. BASIC AND DILUTED EARNINGS PER SHARE	23
8. TRADE AND OTHER RECEIVABLES	24
9. INVENTORIES	24
10. INVESTMENT PROPERTY.....	25
11. LOANS AND BORROWINGS	25
12. TRADE AND OTHER PAYABLES	25
13. TRANSACTIONS AND BALANCES WITH RELATED PARTIES	26
14. CONTINGENT ASSETS AND LIABILITIES.....	27
15. EVENTS AFTER THE REPORTING PERIOD	32
16. STRUCTURE OF ARCO VARA GROUP	33
STATEMENT BY THE MANAGEMENT BOARD	34

Directors' report

Arco Vara group

Arco Vara AS and other entities of Arco Vara group (the "Group") are engaged in various aspects of the real estate business. The Group's three business lines – services, development and construction have been organised into corresponding divisions that provide a wide range of real estate services.

At the end of the second quarter of 2011, the Group comprised 28 subsidiaries (30 June 2010: 28) and 5 joint ventures (30 June 2010: 6).

The performance of all divisions is subject to seasonal fluctuations. The transaction volumes of the Service division usually increase in autumn and spring and the Construction division's turnover and the Development division's investment volumes decline in the winter.

The Service division is engaged in real estate brokerage, valuation, management and consulting as well as short-term investment in residential real estate.

The Development division develops complete living environments and commercial real estate. Fully developed housing solutions are sold to the end-consumer. Commercial properties are developed until they start generating cash flow after which they are sold to a real estate fund or another developer. Despite the strategy, the Group is currently holding some income-yielding commercial properties because they have not been developed to their full potential.

The Construction division provides general construction and environmental engineering services, operating as a general contractor and construction manager as well as a subcontractor.

The Group regards Estonia, Latvia and Bulgaria as its home markets.

Mission, vision and shared values

The mission of Arco Vara is **to be a comprehensive and valued provider of real estate solutions.**

The vision of Arco Vara is **to become a symbol of real estate.**

Our core values include:

Partnership – our client is our partner

Reliability – we are reliable, open and honest

Professionalism – we deliver quality

Consideration – we value our clients as individuals

Responsibility – we keep our promises

GROUP STRUCTURE

Company	Domicile	Group's ownership interest	
		30 June 2011	31 December 2010
%			
Service segment			
Subsidiaries			
Arco Real Estate EOOD ¹	Bulgaria	100	100
Arco Real Estate AS	Estonia	100	100
Arco Vara Kinnisvarabüroo ¹	Estonia	100	100
Adepto SIA ¹	Latvia	80	80
Arco Real Estate SIA ¹	Latvia	80	80

Company	Domicile	Group's ownership interest	
		30 June 2011	31 December 2010
%			
Development segment			
Subsidiaries			
Arco Invest EOOD ¹	Bulgaria	100	100
Arco Facility Management EOOD ¹	Bulgaria	100	100
Arco Project EOOD ¹	Bulgaria	100	100
Alasniidu LA OÜ ¹	Estonia	sold	100
Arco Investeeringute AS	Estonia	100	100
Arco Vara Riia Valduste OÜ ¹	Estonia	100	100
Arco Vara Ärikinnistute OÜ	Estonia	100	100
Fineprojekti OÜ ¹	Estonia	100	-
Kerberon OÜ ¹	Estonia	100	100
Koduküla OÜ ¹	Estonia	100	50
Kolde AS ¹	Estonia	100	100
Lilletee LA OÜ ¹	Estonia	100	100
Pärnu Turg OÜ ¹	Estonia	100	100
T53 Maja OÜ ¹	Estonia	100	100
Waldrop Investments OÜ ¹	Estonia	100	100
Arco Development SIA ¹	Latvia	70	99.9
Ulmana Gatves Nami SIA ¹	Latvia	70	99.9
Arco Invest UAB ¹	Lithuania	100	100
Arco Development UAB ¹	Lithuania	100	100
Arco Capital SRL ¹	Romania	100	100
Arco Investments TOV ¹	Ukraine	75	75
Joint ventures			
Arco HCE OÜ ¹	Estonia	50	50
Tivoli Arendus OÜ ¹	Estonia	50	100
AD Saulkrasti SIA ¹	Latvia	35	50
Bišumižās Nami SIA ¹	Latvia	49.38	49.38
Sporting Riga SIA ¹	Latvia	49.38	49.38
Construction segment			
Subsidiaries			
Arco Ehitus OÜ	Estonia	100	100
AE Ehitusjuhtimine OÜ ¹	Estonia	100	100
Tempera Ehitus OÜ ¹	Estonia	bankrupt	bankrupt

¹Interest through a subsidiary

CHANGES IN GROUP STRUCTURE

On 7 February 2011, Arco Investeeringute AS, a wholly-owned subsidiary of Arco Vara AS, divested 29.99% of its ownership interest in Arco Development SIA to SL Development SIA. The sales price of the shares was 104 euros.

On 18 March 2011, Arco Investeeringute AS, a wholly-owned subsidiary of Arco Vara AS, sold 50% of its stake in Tivoli Arendus OÜ. As a result of the transaction, the interest of Arco Investeeringute AS in Tivoli Arendus OÜ decreased from 100% to 50%. The transaction was conducted at the nominal value of the shares.

On 26 April 2011, Arco Investeeringute AS, a wholly-owned subsidiary of Arco Vara AS, established Fineprojekti OÜ, a wholly-owned subsidiary with a share capital of 2,500 euros.

On 27 May 2011, Arco Vara Kinnisvarabüroo AS increased its interest in Koduküla OÜ from 50% to 100%. The additional 50% stake in Koduküla OÜ was acquired for 1 euro.

Changes in Group structure after the reporting period:

On 5 July 2011, Arco Investeeringute AS, a wholly-owned subsidiary of Arco Vara AS, established a wholly-owned subsidiary, SIA Mārsili II, with a share capital of 1.071 million Latvian lats (1.5 million euros). The subsidiary's share capital was paid in with a non-monetary contribution consisting of the plots of the Baltezers 5 project that used to belong to Arco Investeeringute AS.

On 29 July 2011, Arco Investeeringute AS, a wholly-owned subsidiary of Arco Vara AS, established a 70% subsidiary, Prime Capital SIA, whose share capital is 2,000 Latvian lats (2,846 euros).

KEY PERFORMANCE INDICATORS

- The Group ended the first six months of 2011 with revenue of 23.5 million euros. The figure includes 8.3 million euros earned on the sale of the Tivoli properties to the Group's joint venture Tivoli Arendus OÜ. Excluding the latter transaction, the Group's revenue was 15.2 million euros, a 43% improvement on the first half of 2010.
- Operating loss for the first half-year was 1.4 million euros, a 40% increase year over year.
- Net loss for the first half-year was 1.9 million euros, 69% up on the first half of 2010.
- Equity to assets ratio at period-end was 39.1% (30 June 2010: 37.1%). Return on equity (12 months rolling) was negative (Q2 2010: negative). Return on invested capital (12 months rolling) was 1.3% (Q2 2010: negative).
- At the end of the second quarter, the Group's order backlog stood at 13.5 million euros compared with 6.0 million euros at the end of the second quarter of 2010.
- During the first six months of 2011, the Group sold 56 apartments and plots (HY1 2010: 53 apartments and plots).

	HY1 2011	HY1 2010	Q2 2011	Q2 2010
In millions of euros				
Revenue and other income	23.5	8.9	10.3	4.5
Operating loss	-1.4	-1.0	-0.5	-0.4
<i>Of which net loss on changes in the values of investment properties and inventories</i>	0.0	-0.4	0.0	-0.1
Loss before tax	-1.9	-1.1	-0.6	-0.4
<i>Of which net gain/ loss on the disposal of financial assets</i>	0.3	-0.2	0.3	0.1
Net loss	-1.9	-1.1	-0.6	-0.4
EPS (in euros)	-0.41	-0.24	-0.13	-0.08
Total assets at period-end	64.9	74.5		
Invested capital at period-end	51.1	62.3		
Net loans at period-end	23.5	32.3		
Equity at period-end	25.4	27.6		
Average loan term (in years)	2.0	1.5		
Average interest rate of loans (per year)	7.4%	6.1%		
ROIC (rolling, 4 quarters)	1.3%	neg		
ROE (rolling, 4 quarters)	neg	neg		
Number of staff at period-end	142	153		

FORMULAS USED

Invested capital = current interest-bearing liabilities + non-current liabilities + equity (at end of period)

Net loans = current interest-bearing liabilities + non-current liabilities – cash and cash equivalents – short-term investments in securities (at end of period)

Equity to assets ratio = equity at end of period / total assets at end of period

Average equity = past four quarters' equity at end of period / four

Return on equity (ROE) = past four quarters' net profit / average equity

Average invested capital = past four quarters' current interest-bearing liabilities, non-current liabilities and equity / four

Return on invested capital (ROIC) = past four quarters' profit before tax and interest expense / average invested capital

Earnings per share (EPS) = net profit attributable to owners of the parent / (weighted average number of ordinary shares outstanding during the period – own shares)

Group Chief Executive's review

Compared with the same period last year, the Group's revenue has grown significantly across all divisions and profitability has started to improve. After an interval of several years, the Service division posted an operating profit while the operating loss of the Development division remained at the same level as last year. The biggest setback was the exceptional losses of the Construction division, which is operating in an industry ravaged by rapid inflation that began spiralling in 2010 and counterparty bankruptcies triggered by the economic crisis. Excluding the impact of exceptional losses, the Group ended the second quarter with a profit.

In the first six months of 2011, 56 apartments and plots were sold in the projects of Arco Vara: 38 in Estonia, 9 in Latvia and 9 in Bulgaria. Major ongoing development projects include the Tivoli apartment building in Tallinn, which is in the design phase, and the Manastirski apartment building in Sofia, which is in the construction phase. The Group continues to sell apartments in the Kodukolde community being developed in Tallinn and is completing the sale of plots at Merivälja. In the second quarter, the Development division successfully completed and delivered to the investor the Alasniidu nursery school and commenced the Lille tee nursery school design and build project. Since the reporting date, the Group's Latvian associate has won an auction for the purchase of 86 hectares of residential land in the Mazais Baltezers project that previously could only be used under a lease. The success at the land auction is an important step in securing the Group's position in the Latvian market. The Group continued developing the Bišumuiža 1 apartment project and selling plots in Riga as well as delivering apartments under real right contracts and letting the last vacant rental premises in the Madrid project in Sofia, Bulgaria.

For the Service division, the first half of 2011 was better than the same period in several previous years. Revenue grew and the division ended the half-year with an operating profit of 44 thousand euros compared with an operating loss of 161 thousand euros for the first half of 2010. The number of brokerage transactions increased by 23% and the number of valuation reports issued grew by 39% year over year. At the same time, the number of brokers decreased and the number of appraisers grew by only 11%.

In the first six months of 2011, the Group secured new construction contracts of 4.3 million euros. Our order backlog as at 30 June 2011 was 13.5 million euros against 6.0 million euros at the end of the second quarter of 2010. After the reporting date, the Construction division has completed the Estonian Aviation Academy building in Tartu, the largest project for which Arco Ehitus was the sole general contractor in 2011. The operating loss of the division is attributable to the bankruptcies of two major business partners. Owing to the bankruptcy of construction company K&H the Construction division did not receive payment for work done in Tartu (the receivables are secured with mortgages), and because of the bankruptcy of construction company Kristiine Ehitus in Tallinn the division as the remaining consortium partner had to complete under unfavourable terms construction work started but not completed on account of the bankruptcy.

Within the past 12 months, the Group's loans and borrowings have decreased by 8.8 million euros and equity to assets ratio has risen from 37% to 39%. The weighted average interest rate of loans and borrowings has increased because of a rise in EURIBOR. The Group has responded by lengthening the weighted average duration of loans and borrowings through current refinancing.

REVENUE AND PROFIT

	HY1 2011	HY1 2010	Q2 2011	Q2 2010
In millions of euros				
Revenue				
Service	1.1	0.9	0.6	0.4
Development	14.0	4.6	4.1	2.3
Construction	8.5	3.4	5.6	1.8
Eliminations	-0.1	-0.2	-0.1	0.0
Total revenue	23.5	8.7	10.2	4.5
Operating profit/loss				
Service	0.1	-0.2	0.1	-0.1
Development	-0.2	-0.2	0.4	0.0
Construction	-0.8	0.0	-0.7	0.1
Eliminations	0.2	0.4	0.1	0.1
Unallocated expenses	-0.7	-1.0	-0.4	-0.5
Total operating loss	-1.4	-1.0	-0.5	-0.4
Interest income and expense	-0.7	-0.3	-0.4	-0.1
Other finance income and expenses	0.2	0.2	0.3	0.1
Income tax expense	0.0	0.0	0.0	0.0
Net loss	-1.9	-1.1	-0.6	-0.4

Finance income and expenses was influenced the most by growth in interest expense, which resulted from the completion of the Madrid project and discontinuance of capitalisation of associated borrowing costs. In the first half of 2011, the Group did not earn any exceptional finance income or incur any exceptional finance expenses but the result for the first quarter of 2010 was influenced by foreign exchange gain of 0.15 million euros earned on a receivable from AS Ühendatud Kapital that was denominated in US dollars and a loss of 0.23 million euros incurred on the disposal of Arco Vara Saare Kinnistute OÜ.

CASH FLOWS

	HY1 2011	HY1 2010
In millions of euros		
Cash flows from operating activities	-1.1	0.1
Cash flows from investing activities	0.1	0.8
Cash flows from financing activities	-1.0	-2.6
Net cash flow	-2.0	-1.7
Cash and cash equivalents at beginning of period	4.2	4.1
Effect of movements in exchange rates	0.0	-0.2
Cash and cash equivalents at end of period	2.2	2.3

In March 2011, Arco Investeeringute AS repaid ahead of schedule the remaining 5.27 million euros of the loan taken from SEB Pank for acquiring the land under the Tivoli project and 0.12 million euros of the loan taken for acquiring the land under the Laeva project. Repayment of the Tivoli loan and partial repayment of the Laeva 2 loan are not reflected in the Group's cash flows because the buyer of Tivoli Arendus OÜ paid the cash directly to SEB. There have been no other exceptional loan settlements in 2011.

Interest payments accounted for 0.6 million euros of the net cash outflow from financing activities. Scheduled and inventory sales-related settlements of loan principal totalled 1.2 million euros. The largest proportion of credit limits utilised during the period was related to the construction of the last but one phase in the Kodukolde project and the Alasniidu and Lille tee nursery schools that accounted for 2.5 million euros of the total. Use of the Kodukolde credit limit is not reflected in the cash flows because invoices received from Merko Ehitus are booked as a loan and there are no cash movements.

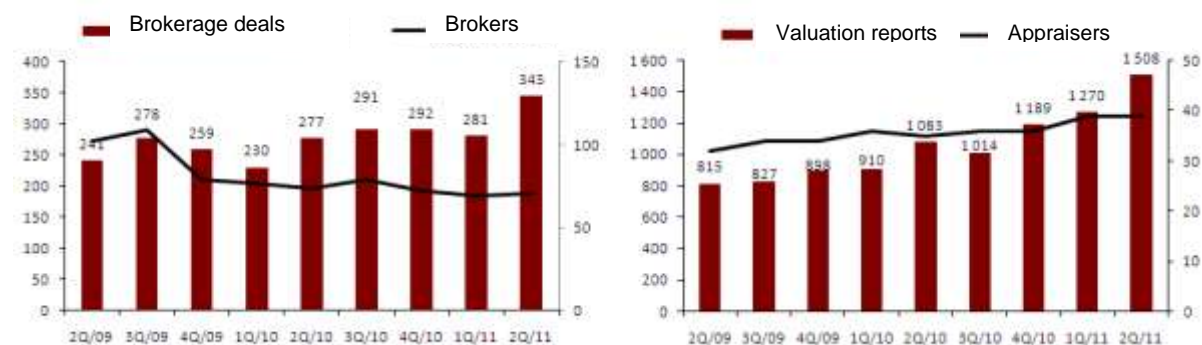
The largest current liabilities to be settled in the next 12 months comprise:

- estimated principal repayments to be made on the sale of reserved premises and payments under the settlement schedule of the loan taken for the Boulevard Residence Madrid project in Sofia of 4.7 million euros;
- repayments of the loan taken for the Manastirski project of 2.2 million euros;
- repayments of an investment loan taken for a cash flow project at Kadaka tee 131 of 1.4 million euros;
- repayments of the loan taken for the Bišumuiža project of 1.3 million euros;
- repayments of the loan taken for the Laeva 2 development project of 1.1 million euros.

In the first six months of 2011, the Group made regular repayments under the loans taken for the Kodukolde project in Tallinn, the Bišumuiža 1 project in Riga and the Madrid project in Sofia and scheduled settlements under the loans taken for its cash flow generating projects. The Group is also following the principal repayment schedules set for the loans taken for the Laeva 2 project and Koduküla OÜ.

SERVICE DIVISION

In 2011, the performance of the Service division has been in every respect better than in 2010. The division ended the first half-year with an operating profit of 44 thousand euros compared with an operating loss of 161 thousand euros for the first half of 2010. The number of the Group's brokerage transactions increased by 23% and the number of valuation reports issued grew by 39% year over year. At the same time, the number of brokers decreased and the number of appraisers grew by only 11%.



	HY1 2011	HY1 2010	Change, %
Number of brokerage transactions	626	507	23%
Number of projects on sale	173	177	-2%
Number of valuation reports	2,778	1,993	39%
Number of appraisers*	39	35	11%
Number of brokers*	71	74	-4%
Number of staff at end of period	46	59	-22%

* Includes people working under service contracts.

DEVELOPMENT DIVISION

In the first six months of 2011, 56 apartments and plots were sold in the projects of Arco Vara. The Development division sold seven apartments in the Bišu muiža project and two plots in the Baltezers project in Latvia, 36 apartments in the Kodukolde project and two plots in the Merivälja project in Estonia, and nine apartments in the Madrid project in Sofia, Bulgaria.

The Group succeeded in finding a partner, International Invest Project OÜ, for the Tivoli project and raised financing for the construction of phase I. Design work is under way and construction should start in 2011.

The last but one phase of the Kodukolde development project (50 apartments) was completed in June. Revenue for the first half-year includes the sale of 29 apartments of this phase.

Construction of the last phase (48 apartments) commenced in the second quarter. Construction work is performed and financed by AS Merko Ehitus. The buildings are expected to be completed in the first half of 2012.

The building of the Alasniidu nursery school was granted a use permit at the end of May and was delivered to Harku local government with whom a rental agreement had been signed. The company that owns the nursery school was sold in the second quarter of 2011 and with this the project was successfully completed.

At the end of the first quarter, a wholly-held subsidiary of Arco Investeeringute AS bought the right of superficies to a property in Lille tee in Viimsi with a view to building a nursery school for six groups of children. The Group has already signed a long-term rental agreement with the local government. According to plan, the nursery school should be completed in the first quarter of 2012. Construction work is performed by YIT.

In Bulgaria, the construction of phase I of the Manastirski project is under way: 42% of the apartments have already been reserved. In the commercial and residential building Boulevard Residence Madrid in Sofia the division continues delivering reserved apartments under real right contracts and selling the remaining free apartments.

At the end of June 2011, the Development division employed 21 people (30 June 2010: 26).

For further information on our projects, please refer to: www.arcorealestate.com/development.

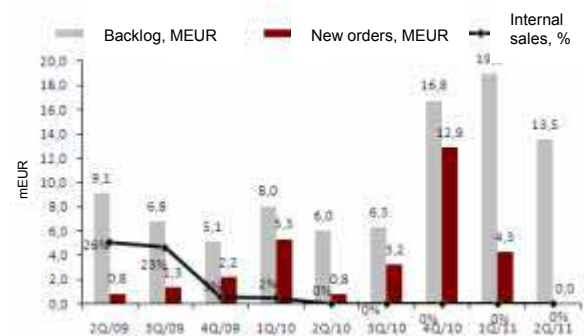
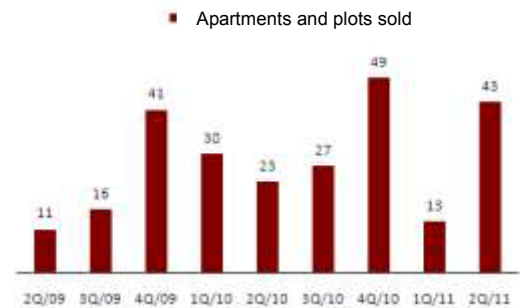
CONSTRUCTION DIVISION

The Construction division is typically actively involved in environmental, infrastructure and civil engineering (mostly educational establishments-related) projects.

As at the end of the second quarter of 2011, the largest active construction contracts comprised the construction of the Tallinn-Muuga water and wastewater networks and facilities with the remaining balance of 5.1 million euros, the design and build of the water and wastewater networks of the Jõgeva and Puurmani rural municipalities with the remaining balance of 2.3 million euros and the water management project for the wastewater collection area of Tamsalu with the remaining balance of 1.4 million euros.

In the first half of 2011, the division secured new construction contracts of 4.3 million euros. As at the reporting date, the order backlog stood at 13.5 million euros compared with 6.0 million euros at the end of the second quarter of 2010.

At the end of June 2011, the Construction division employed 55 people (30 June 2010: 47).



SUMMARY TABLE OF MAJOR PROJECTS

Project type	Name	Location	Legal interest	Building rights according to business plan	Current status	Classification in the statement of financial position
Commercial	Ahtri tn 3	Estonia, Tallinn	50%	48,518m ²	The old plan is in force. A detailed plan for more extensive building rights is in the final stages of adoption. In the new plan, above-ground building rights extend to 51,100m ² .	Investments
Commercial	Laeva 2	Estonia, Tallinn	100%	7,776 m ²	A detailed plan has been adopted. A building permit has been obtained. Tenant search is under way.	Investment property
Commercial	Lilletee	Estonia, Viimsi rural municipality	100%	1,748 m ²	A right to superficies with the obligation to build a nursery school for six groups of children has been obtained. Design work is under way.	Inventories
Project type	Name	Location	Legal interest	Rentable area	Current status	Classification in the statement of financial position
Cash flow	Kerberon	Estonia, Tallinn	100%	13,236 m ²	Building rights and the right to superficies have been obtained. Generates cash flow.	Investment property
Cash flow	Madrid	Bulgaria, Sofia	100%	6,950 m ²	Building rights have been obtained. Generates cash flow.	Investment property
Cash flow	Pärnu market	Estonia, Pärnu	100%	2,529 m ²	Building rights have been obtained. Generates cash flow.	Investment property
Project type	Name	Location	Legal interest	Building rights according to business plan	Current status	Classification in the statement of financial position
Apartments	Bišumuiža 1	Latvia, Riga	70%	Area of unsold apartments 12,924 m ²	Building rights have been obtained. Sale of apartments is under way. In 2010 we started completing apartments of phase II.	Inventories
Apartments	Bišumuiža 2	Latvia, Riga	49%	87,737 m ²	Building rights have been obtained. Design work is under way.	Investments
Apartments	Hills	Lithuania, Vilnius	100%	6,500 m ²	Building rights have been obtained. On sale.	Inventories
Apartments	Kolde	Estonia, Tallinn	100%	Area of unsold/unreserved apartments 3,019 m ²	The right to superficies and building rights have been obtained. Sale of apartments and construction of the last but one phase are under way.	Inventories
Apartments	Madrid	Bulgaria, Sofia	100%	Area of unsold/unreserved apartments 2,563 m ² .	The building is complete, sales continue. One apartment has been rented out.	Inventories
Apartments	Manastirski	Bulgaria, Sofia	100%	Area of unsold/unreserved apartments 24,216 m ²	Building rights have been obtained. Construction and sales are under way.	Inventories
Apartments	Paldiski mnt 70c	Estonia, Tallinn	33%	ca 34,000 m ²	The initial planning outline is under preparation.	Investment property
Apartments	Tehnika tn 53	Estonia, Tallinn	100%	1,515 m ²	A detailed plan has been adopted, design work is under way.	Inventories
Apartments	Tivoli	Estonia, Tallinn	50%	58,470 m ²	A detailed plan has been adopted, design work is under way.	Investments
Plots	Baltezers-3	Latvia, Riga	70%	604,674 m ² residential land	The right to superficies has been obtained. 188 plots. Preparations for the construction of phase I infrastructure are under way (phase I comprises 33 plots).	Investment property
Plots	Baltezers-5	Latvia, Riga	100%	No of unsold plots 23	Building rights have been obtained. Construction has been completed. On sale.	Inventories
Plots	Merivälja 2	Estonia, Merivälja	100%	Unsold/unreserved 3,451 m ² , 3 plots	Roads and networks have been completed. Sale of plots is under way.	Inventories
Plots	Palusambla 1	Estonia, Nõmme	100%	55,466 m ²	A detailed plan for the formation of 12 plots for one detached building each is in the final phase of adoption.	Inventories
Plots	Pärtli	Estonia, Saue	100%	84 plots, average plot 1,500 m ²	No building rights. The detailed plan process is under way. Is awaiting an improvement in the market situation.	Investment property
Plots	Tooma	Estonia, Saue	100%	107 plots, average plot 1,802 m ²	No building rights. The detailed plan process is under way. Is awaiting an improvement in the market situation	Inventories
Plots	Vahi	Estonia, Vääna	100%	21 plots, average plot 3,363 m ²	Building rights have been obtained. Construction design documentation has been prepared. Is awaiting an improvement in the market situation.	Inventories

Note: The development and success of the Group's development projects depend largely on external factors, particularly the adoption of plans and the issuance of building permits by the local government and the planning authorities. The information presented in the table, such as building rights according to business plan, current status, project type and classification of the project in the statement of financial position, has been recorded based on management's intentions and best judgment and may change in line with changes in the planning process. Expectations of the projects' realisation may also change over time in connection with changes in the market and the competition environment. Management estimates the value of the project portfolio on an ongoing basis and is prepared to sell any project or part of a project at any time, depending on the results of the cost-benefit analysis.

The projects presented in the summary table account for the following portions of the Group's assets:

Line item in the statement of financial position	Balance of line item at 30 June 2011	Carrying amount of projects presented in the summary table of major projects at 30 June 2011
In millions of euros		
Total assets	64.9	46.7
Inventories	26.0	25.2
Investment property	22.2	21.5
Investments	1.0	0.0

SIGNIFICANT CHANGES IN DETAILED PLANS DURING THE FIRST SIX MONTHS OF 2011

Tehnika 53: A detailed plan for the property was initiated on 30 January 2002 for determining building rights. On 7 January 2004, Tallinn City Government approved the detailed plan and put it on public display. Owing to an objection lodged during public display, the adoption proceedings halted until 2009. To date, an updated version of the plan has been adjusted to effective legislation and has been approved by all relevant authorities. The detailed plan has also passed a new public hearing during which three submissions/objections were lodged, all of which have been removed. On 10 November 2010, the Tallinn City Government sent the plan for official adoption to the Tallinn City Council. The Tallinn City Council adopted the detailed plan on 2 December 2010 and the detailed plan took effect on 2 January 2011.

PEOPLE

At the end of the second quarter of 2011, the Group employed 142 people compared with 153 at the end of the second quarter of 2010. Employee remuneration expenses for the first half-year totalled 1.8 million euros against 1.7 million euros for the first half of 2010.

The remuneration of the member of the parent company's management board for the first six months of 2011 amounted to 0.07 million euros compared with 0.08 million euros for the first half of 2010.

Since 5 September 2009, the Group's management board has had one member - Lembit Tampere

SHARE AND SHAREHOLDERS

Arco Vara AS has issued a total of 4,741,707 shares. At 30 June 2011, the company had 1,945 shareholders and the share price closed at 4.34 euros, a 21% decrease since the previous year-end.

The following charts reflect movements in the Arco Vara share price and daily turnover in the first half of 2011:
In euros (EUR)



Changes in share price compared with the benchmark index OMX Tallinn in the first half of 2011:



Index/equity	1 Jan 2011	30 June 2011	+/-%
—OMX Tallinn	698.38	644.09	-7.77
—ARC1T	EUR 5.51	EUR 4.34	-21.31

Major shareholders at 30 June 2011	Number of shares	Interest, %
HM INVESTEERINGUD OÜ	1,038,632	21.9%
TOLETUM OÜ	1,037,975	21.9%
Baltplast OÜ	897,135	18.9%
GAMMA HOLDING OÜ	437,976	9.2%
Skandinaviska Enskilda Banken Ab Clients	219,585	4.6%
FIREBIRD REPUBLICS FUND LTD	205,064	4.3%
Central Securities Depository of Lithuania	132,382	2.8%
FIREBIRD AVRORA FUND, LTD.	106,897	2.4%
SWEDBANK AB CLIENTS	24,000	0.5%
Other	642,061	13.5%
Total	4,741,707	100.0%

Holdings of members of the management and supervisory boards at 30 June 2011	Position	Number of shares held	Interest, %
Lembit Tampere	Member of Management Board	0	0%
Richard Tomingas (Toletum OÜ)	Chairman of Supervisory Board	1,037,975	21.9%
Hillar-Peeter Luitsalu (HM Investeeringud OÜ, close family members)	Member of Supervisory Board	1,048,139	22.1%
Aare Tark	Member of Supervisory Board	0	0%
Kalev Tanner	Member of Supervisory Board	0	0%
Ragnar Meitern	Member of Supervisory Board	0	0%
Total		2,086,114	44.0%

DESCRIPTION OF THE MAIN RISKS

Credit risk

Credit risk exposure is the greatest at the Construction division. Accordingly, counterparties' settlement behaviour is monitored on an ongoing basis.

Liquidity risk

The Group's free funds are placed in overnight or short-term fixed-interest term deposits with the largest banks operating in Estonia. The duration of a term deposit is generally one week. Owing to high refinancing risk, cash flow management is tight. The Group's cash and cash equivalents balance is constantly smaller than the balance of loans that require refinancing in the next 12 months. At 30 June 2011, the weighted average duration of interest-bearing liabilities was 2.0 years, which means that on average all loans need to be refinanced every two years. Although at the end of the second quarter of 2011 the Group's cash and cash equivalents totalled 2.2 million euros, 1.5 million euros of this was under the Group's own control but the rest was in accounts with restricted withdrawal opportunities (mostly accounts of designated purpose where withdrawals require the bank's consent). Liquidity and refinancing risks continue to be the most significant risks for the Group.

Interest rate risk

The base currency of most of the Group's loan agreements is the euro and the base interest rate is 3 or 6 month EURIBOR. As a result, the Group is exposed to developments in international capital markets. At the moment, the Group does not use hedging instruments to mitigate its long-term interest rate risk. In the first six months of 2011, the Group's interest-bearing liabilities decreased by 5.9 million euros to 25.0 million euros at 30 June 2011. The period's interest payments on interest-bearing liabilities totalled 0.5 million euros. Compared with the end of the second quarter of 2010, the weighted average interest rate has risen from 6.1% to 7.4%.

Currency risk

Purchase and sales contracts are mostly signed in local currencies: euros (EUR), Latvian lats (LVL) and Bulgarian lev (BGN). The Group is not protected against currency devaluations. After the adoption of the euro in Estonia from 1 January 2011, the currency risk arising from the exchange rate of the Estonian kroon and the euro ceased to exist. Most liquid funds are held in short-term deposits denominated in euros.

The management board confirms that the directors' report provides a true and fair view of the development, financial performance and financial position of Arco Vara group as well as a description of the main risks and uncertainties.



Lembit Tampere

Chief Executive Officer
and Member of the Management Board

26 August 2011

Condensed consolidated interim financial statements

Consolidated statement of comprehensive income

For the period ended 30 June	Note	HY1 2011	HY1 2010	Q2 2011	Q2 2010
In thousands of euros					
Revenue from rendering of services		10,340	4,200	6,603	2,365
Revenue from sale of goods		13,167	4,507	3,645	2,113
Total revenue	2	23,507	8,707	10,248	4,478
Cost of sales	3	-22,434	-7,637	-9,742	-3,892
Gross profit		1,073	1,070	506	586
Other income		12	183	7	66
Distribution expenses	4	-214	-159	-112	-97
Administrative expenses	5	-2,240	-1,942	-879	-842
Other expenses		-59	-172	-16	-104
Operating loss		-1,428	-1,020	-494	-391
Finance income	6	417	580	383	354
Finance expenses	6	-908	-668	-487	-320
Loss before tax		-1,919	-1,108	-598	-357
Income tax expense		0	-28	0	-27
Loss for the period		-1,919	-1,136	-598	-384
<i>Loss attributable to owners of the parent</i>		-1,932	-1,136	-598	-384
<i>Profit attributable to non-controlling interests</i>		13	0	0	0
Other comprehensive income					
Exchange differences on translating foreign operations		0	12	0	1
Total comprehensive expense for the period		-1,919	-1,124	-598	-383
<i>Total comprehensive expense attributable to owners of the parent</i>		-1,919	-1,124	-598	-383
<i>Total comprehensive income/expense attributable to non-controlling interests</i>		0	0	0	0
Earnings per share (in euros)	7				
- Basic		-0.41	-0.24	-0.13	-0.08
- Diluted		-0.41	-0.24	-0.13	-0.08

Consolidated statement of financial position

	Note	As at 30 June 2011	As at 31 December 2010
In thousands of euros			
Cash and cash equivalents		2,234	4,209
Trade and other receivables	8	9,494	5,760
Prepayments		392	192
Inventories	9	26,001	35,740
Total current assets		38,121	45,901
Investments		997	996
Trade and other receivables	8	2,950	76
Investment property	10	22,163	22,887
Property, plant and equipment		665	703
Intangible assets		20	20
Total non-current assets		26,795	24,682
TOTAL ASSETS		64,916	70,583
Loans and borrowings	11	13,726	27,126
Trade and other payables	12	8,240	4,813
Deferred income		4,379	4,859
Provisions		1,158	1,378
Total current liabilities		27,503	38,176
Loans and borrowings	11	11,323	3,855
Other payables	12	710	724
Total non-current liabilities		12,033	4,579
TOTAL LIABILITIES		39,536	42,755
Share capital		3,030	3,030
Statutory capital reserve		2,011	2,011
Retained earnings		20,339	22,787
Total equity		25,380	27,828
Equity attributable to non-controlling interests		175	-70
Equity attributable to equity holders of the parent		25,205	27,898
TOTAL LIABILITIES AND EQUITY		64,916	70,583

Consolidated statement of cash flows

For the period ended 30 June	Note	HY1 2011	HY1 2010
In thousands of euros			
Loss for the period		-1,919	-1,135
Interest income and interest expense, net	6	720	268
Gain/loss on sale of subsidiaries and interests in joint ventures	6	-284	88
Gain/loss on other long-term investments	6	52	0
Impairment losses on financial assets	6	0	9
Depreciation, amortisation and impairment losses on property, plant and equipment and intangible assets	3, 5	49	58
Change in the fair value of investment property	10	0	1
Gain/loss on the sale of investment property	10	0	21
Gain/loss on inventory write-downs and reversals of inventory write-downs	3	0	355
Foreign exchange gains and losses	6	3	-370
Income tax expense		0	-1
Operating cash flow before working capital changes		-1,379	-706
Change in receivables and prepayments		3,216	813
Change in inventories		1,955	181
Change in payables and deferred income		-4,913	-178
NET CASH USED IN/FROM OPERATING ACTIVITIES		-1,121	110
Acquisition of property, plant and equipment and intangible assets		-9	-22
Paid on development of investment properties		-729	-11
Proceeds from sale of investment properties		177	1,520
Acquisition of subsidiaries and interests in joint ventures		1	0
Proceeds from disposal of subsidiaries and interests in joint ventures		891	7
Loans granted		-362	-668
Repayment of loans granted		50	0
Interest received		113	11
NET CASH FROM INVESTING ACTIVITIES		132	837
Proceeds from loans received		1,301	3,874
Settlement of loans and finance lease liabilities		-1,680	-5,412
Interest paid		-607	-1,067
NET CASH USED IN FINANCING ACTIVITIES		-986	-2,605
NET CASH FLOW		-1,975	-1,658
Cash and cash equivalents at beginning of period		4,209	4,137
Decrease in cash and cash equivalents		-1,975	-1,658
Effect of exchange rate fluctuations on cash held		0	-176
Cash and cash equivalents at end of period		2,234	2,303

Consolidated statement of changes in equity

	Equity attributable to equity holders of the parent					Non-controlling interests	Total equity
	Share capital	Statutory capital reserve	Own shares	Retained earnings	Total		
In thousands of euros							
Balance at 31 December 2009	60,898	2,011	-255	-34,475	28,179	-76	28,103
Reduction of share capital	-57,868	0	255	57,613	0	0	0
Total comprehensive expense for the period				-1,124	-1,124		-1,124
Balance at 30 June 2010	3,030	2,011	0	22,014	27,055	-76	26,979
Balance at 31 December 2010	3,030	2,011	0	22,857	27,898	-70	27,828
Change in non-controlling interests(through change in interests in subsidiaries)				-232	-232	232	0
Effect of acquisition of a subsidiary				-529	-529		-529
Total comprehensive Income/expense for the period				-1,932	-1,932	13	-1,919
Balance at 30 June 2011	3,030	2,011	0	20,164	25,205	175	25,380

Notes to the condensed consolidated interim financial statements

1. Significant accounting policies

The unaudited condensed consolidated interim financial statements of Arco Vara AS for the second quarter and first six months of 2011 have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union. The condensed consolidated interim financial statements have been prepared in accordance with IAS 34 *Interim Financial Reporting*, using the same accounting policies and measurement bases that were applied in preparing the consolidated financial statements as at and for the year ended 31 December 2010.

The financial statements are presented in euros. The figures in the tables are in thousands of currency units unless otherwise indicated.

2. Segment reporting by business segments

The Group is organised into the following business segments:

Development - real estate development: development of residential and commercial environments and long-term investment in real estate;

Service - real estate services: real estate brokerage, valuation, management and short-term investment in real estate;

Construction - general and sub-contracting and construction supervision in the field of buildings construction and civil and environmental engineering.

Segment	Development ¹		Service		Construction		Unallocated items		Eliminations		Consolidated	
	HY1 2011	HY1 2010	HY1 2011	HY1 2010	HY1 2011	HY1 2010	HY1 2011	HY1 2010	HY1 2011	HY1 2010	HY1 2011	HY1 2010
In thousands of euros												
External revenue	13,981	4,667	1,007	712	8,515	3,328	4	0	0	0	23,507	8,707
<i>Change</i>	200%	62%	41%	-33%	156%	-53%					170%	-21%
Inter-segment revenues	3	3	138	147	0	31	0	0	-141	-181	0	0
Total revenue	13,984	4,670	1,145	859	8,515	3,359	4	0	-141	-181	23,507	8,707
Operating profit/loss	-227	-218	44	-161	-768	19	-702	-1,048	225	388	-1,428	-1,020
<i>Of which inventory write-downs and reversals of inventory write-downs, net</i>	0	-355	0	0	0	0			0	0	0	-355

Segment	Development		Service		Construction		Unallocated items		Eliminations		Consolidated	
	Q2 2011	Q2 2010	Q2 2011	Q2 2010	Q2 2011	Q2 2010	Q2 2011	Q2 2010	Q2 2011	Q2 2010	Q2 2011	Q2 2010
In thousands of euros												
External revenue	4,093	2,281	555	367	5,597	1,830	3	0	0	0	10,248	4,478
<i>Change</i>	79%	58%	51%	-33%	206%	-44%					129%	-15%
Inter-segment revenues	1	1	84	76	0	0	0	0	-85	-77	0	0
Total revenue	4,094	2,283	639	443	5,597	1,839	3	-10	-85	-77	10,248	4,478
Operating profit/loss	399	-44	76	-74	-708	149	-369	-560	108	138	-494	-391
<i>Of which inventory write-downs and reversals of inventory write-downs, net</i>	0	-145	0	0	0	0	0	0	0	0	0	-145

¹ The revenue of the Development segment for the first half of 2011 includes revenue of 8,309 thousand euros earned on the sale of inventory to the Group's joint venture Tivoli Arendus OÜ on 18 March 2011.

3. Cost of sales

	HY1 2011	HY1 2010	Q2 2011	Q2 2010
In thousands of euros				
Cost of properties sold ¹	-12,310	-3,436	-2,989	-1,593
Cost of construction services purchased	-8,594	-2,660	-5,944	-1,565
Personnel expenses	-912	-660	-489	-362
Management and administration costs	-468	-370	-235	-187
Vehicle expenses	-94	-88	-51	-45
Depreciation, amortisation and impairment losses	-7	-10	-4	-7
Inventory write-down expenses	0	-355	0	-145
Other costs	-49	-58	-30	12
Total cost of sales	-22,434	-7,637	-9,742	-3,892

¹ Includes the acquisition cost of inventories sold to the Group's joint venture Tivoli Arendus OÜ on 18 March 2011 of 8,300 thousand euros.

4. Distribution expenses

	HY1 2011	HY1 2010	Q2 2011	Q2 2010
In thousands of euros				
Advertising expenses	-118	-76	-62	-47
Personnel expenses	-35	-40	-18	-24
Market research expenses	-18	-2	-2	-1
Brokerage fees	-1	-35	-1	-21
Other distribution expenses	-42	-6	-29	-4
Total distribution expenses	-214	-159	-112	-97

5. Administrative expenses

	HY1 2011	HY1 2010	Q2 2011	Q2 2010
In thousands of euros				
Personnel expenses	-862	-958	-434	-465
Legal and consulting fees	-853	-439	-210	-136
Office expenses	-242	-309	-113	-140
Vehicle expenses	-91	-113	-47	-59
Depreciation, amortisation and impairment losses	-42	-45	-21	-22
Expenses from write-down of receivables	-3	-31	-3	8
Other expenses	-147	-47	-51	-28
Total administrative expenses	-2,240	-1,942	-879	-842

6. Finance income and expenses

Finance income	HY1 2011	HY1 2010	Q2 2011	Q2 2010
In thousands of euros				
Gain on sale of investments in subsidiaries	284	58	284	58
Interest income	131	137	97	58
Foreign exchange gains	2	374	2	227
Gain on sale of investments in joint ventures	0	7	0	7
Share of profit of joint ventures	0	4	0	4
Total finance income	417	580	383	354

Finance expenses	HY1 2011	HY1 2010	Q2 2011	Q2 2010
In thousands of euros				
Interest expense	-851	-405	-462	-200
Foreign exchange losses	-5	-5	-1	-14
Losses on sale of investments in joint ventures	0	-152	0	-11
Share of losses of joint ventures	0	-96	0	-88
Losses on sale of investments in subsidiaries	0	-1	0	-1
Other finance expenses	-52	-9	-24	-6
Total finance expenses	-908	-668	-487	-320

7. Basic and diluted earnings per share

Basic earnings per share are calculated by dividing profit or loss attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the period. Under section 283 of the Estonian Commercial Code, own shares do not provide the company with any shareholder rights. Accordingly, they are not included in calculating the weighted average number of ordinary shares.

	HY1 2011	HY1 2010	Q2 2011	Q2 2010
Weighted average number of ordinary shares outstanding during the period	4,741,707	4,741,707	4,741,707	4,741,707
Net loss attributable to equity holders of the parent (In thousands of euros)	-1,932	-1,136	-598	-384
Earnings per share (in euros)	-0.41	-0.24	-0.13	-0.08

Diluted earnings per share are calculated by adjusting the profit or loss attributable to equity holders of the parent and the weighted average number of shares outstanding for the effects of all dilutive potential ordinary shares. At the reporting date the Group did not have any dilutive potential ordinary shares. Therefore, diluted earnings per share equalled basic earnings per share.

8. Trade and other receivables

Current trade and other receivables

	30 June 2011	31 December 2010
In thousands of euros		
Trade receivables		
Trade receivables	5,346	2,320
Allowance for doubtful items	-320	-320
Total trade receivables	5,026	2,000
Other receivables		
Loans granted	2,052	1,753
Miscellaneous receivables	547	659
Total other receivables	2,599	2,412
Accrued income		
Interest receivable	203	198
Due from customers under long-term construction contracts	1,333	429
Prepaid and refundable taxes	327	548
Other accrued income	6	173
Total accrued income	1,869	1,348
Total current trade and other receivables	9,494	5,760

Non-current trade and other receivables

	30 June 2011	31 December 2010
In thousands of euros		
Loans granted ¹	2,878	1
Other long-term receivables	72	75
Total non-current trade and other receivables	2,950	76

¹ A long-term loan to the Group's joint venture Tivoli Arendus OÜ given on the sale of the Tivoli project inventory to Tivoli Arendus OÜ in March 2011.

9. Inventories

	30 June 2011	31 December 2010
In thousands of euros		
Properties purchased and developed for resale	25,683	35,486
Materials and finished goods	120	32
Prepayments to inventory suppliers	198	222
Total inventories	26,001	35,740

10. Investment property

In thousands of euros	
Balance at 31 December 2009	14,005
Acquisitions	0
Sales	-1,376
Transfer from inventories	11,502
Net loss on changes in fair value	-1
Balance at 30 June 2010	24,130
Balance at 31 December 2010	22,887
Acquisitions	55
Capitalised development costs	810
Sales	-1,589
Balance at 30 June 2011	22,163

11. Loans and borrowings

	30 June 2011			31 December 2010		
	Total	Of which current portion	Of which non-current portion	Total	Of which current portion	Of which non-current portion
In thousands of euros						
Bank loans	22,778	11,851	10,927	29,235	26,775	2,460
Finance lease liabilities	37	8	29	45	12	33
Other loans	2,234	1,867	367	1,701	339	1,362
Total	25,049	13,726	11,323	30,981	27,126	3,855

In the first six months of 2011, the Group settled loans and borrowings of 1,680 thousand euros (HY1 2010: 5,412 thousand euros) through cash transactions and received new loans and borrowings of 1,301 thousand euros (HY1 2010: 3,874 thousand euros). As regards non-cash transactions, the Group's loans and borrowings were affected the most by the sale of the Tivoli property to the joint venture Tivoli Arendus OÜ as a result of which the counterparty settled the Group's loan liabilities of 5,387 thousand euros. Other major non-cash movements included the sale of Alasniidu LA OÜ that reduced the Group's loans and borrowings by 1,038 thousand euros and an increase in the Group's stake in Koduküla OÜ (from 50% to 100%) that increased loans and borrowings by 937 thousand euros.

12. Trade and other payables

Current trade and other payables		30 June 2011	31 December 2010
In thousands of euros			
Trade payables		5,662	2,412
Miscellaneous payables		1,083	1,180
Taxes payable			
Value added tax		246	66
Corporate income tax		159	157
Personal income tax		67	61
Social security tax		110	103
Other taxes		45	10
Total taxes payable		627	397

Accrued expenses		
Interest payable	373	127
Payables to employees	235	281
Other accruals	260	416
Total accrued expenses	868	824
Total current trade and other payables	8,240	4,813

Non-current trade and other payables

	30 June 2011	31 December 2010
In thousands of euros		
Interest payable	4	4
Retentions payable	65	79
Other non-current payables	641	641
Total non-current trade and other payables	710	724

13. Transactions and balances with related parties

	For HY1 2011 or as at 30 June 2011	For HY1 2010 or as at 31 December 2010
In thousands of euros		
Transactions and balances with joint ventures		
Revenue	1	1
Current loan receivables	801	1,029
Trade receivables	64	5
Current interest receivables	23	13
Transactions and balances with companies related members of the supervisory board that have a significant interest in the Group's parent company		
Revenue	1	0
Trade receivables	1	0
Current loan receivables	376	376
Current interest receivables	102	92
Transactions and balances with the Group's key personnel		
Other current receivables	24	24
Transactions and balances with other related parties		
Services purchased	-637	-46
Trade receivables	4	6
Current loan receivables	182	182
Current interest receivables	79	75
Trade payables	156	24
Other current payables	318	38
Current loan liabilities	377	640
Current interest liabilities	0	2

14. Contingent assets and liabilities

Claims filed by Arco Vara AS and Arco Ehitus OÜ against Tempera Ehitus OÜ

OÜ Tempera Ehitus was declared bankrupt by a ruling issued by Harju County Court on 26 February 2009.

Arco Vara AS filed its claim on 4 March 2009. The claim of 150 thousand euros was based on a credit agreement signed on 7 August 2008.

Arco Ehitus OÜ filed its claim on 9 March 2009. The claim of 152 thousand euros was based on a loan agreement and site management and construction services agreement.

The first meeting of the creditors was held on 25 March 2009. The meeting decided not to approve the appointment of Maire Arm as the bankruptcy trustee. On 3 April 2009, the creditors submitted to the court a jointly prepared list of desired trustees. On 9 April 2009, the court appointed Katrin Prükk as the new trustee.

On 5 November 2009, the trustee Katrin Prükk imposed an injunction requiring rectification of deficiencies in the proof of claim. Arco Ehitus OÜ and Arco Vara AS rectified the deficiencies outlined in the injunction by 13 December 2009.

On 19 November 2009, Arco Vara AS partially assigned its claim to Leising Grupp OÜ. The claim was assigned to the extent of 32 thousand euros.

The meeting for defending the claims against OÜ Tempera Ehitus (bankrupt) was held on 20 November 2009. The claim of Arco Ehitus OÜ was defended to the extent presented in the proof of claim. The trustee lodged an objection to interest for 2009 of 3 thousand euros claimed by Arco Vara AS. Thus, the claim of Arco Vara AS was defended to the extent of 147 thousand euros.

The bankruptcy trustee's report indicates that the debtor has commitments of 868 thousand euros but no tangible assets. Accordingly, the Group's management board believes that it is unlikely that the claims filed by Arco Vara AS and Arco Ehitus OÜ against OÜ Tempera Ehitus (bankrupt) will be settled.

On 27 September 2010, the creditors' general meeting decided to enlarge the bankruptcy committee by one member.

There were no developments in the above bankruptcy proceedings in the second quarter of 2011.

The bankruptcy proceedings are pending.

Action brought by Indrek Porila against Arco Vara AS

On 13 May 2010, Indrek Porila, a former employee of Arco Vara AS, brought an action against Arco Vara AS at Harju County Court, claiming settlement of a principal liability of 1,342 thousand euros and associated late payment interest of 401 thousand euros, i.e. 1,743 thousand euros in aggregate. In addition, Indrek Porila is claiming a 12.5% stake in Floriston Grupp OÜ that belongs to Arco Vara AS.

Arco Vara AS responded to the action on 3 June 2010. It did not admit the claims, stating that they were in contradiction with the original agreement with Indrek Porila as none of the real estate projects on the basis of which the shareholding was to be divided had realised. On the same date, the Republic of Estonia acting through the Ministry of Finance lodged an appeal against the ruling of Harju County Court under which Indrek Porila had been granted state legal aid. The Ministry had established that Indrek Porila had knowingly provided false information about his financial position as a result of which the state fee payable on the claim had been reduced. The court has not yet ruled on the appeal.

On 9 June 2010, Arco Vara AS filed an application with the court in which it requested security to be provided by Indrek Porila. With a ruling of 13 April 2011 the court decided to partly satisfy the application and obligated Indrek Porila to pay Arco Vara AS 1,600 euros as compensation of procedural costs.

The litigation is pending.

Action brought by Arco Ehitus OÜ through the Ministry of Education and Research against the Republic of Estonia

On 9 March 2010, Järvamaa Education Centre, a state-owned vocational educational institution administered by the Ministry of Education and Research, Arco Ehitus OÜ and OÜ Kristiine Ehitus signed general renovation contract no 1/344 within the framework of a public procurement tender for the renovation of the Paide academic building of Järvamaa Education Centre (procurement reference number 115793) (the Contract). Arco Ehitus OÜ was the co-tenderer and OÜ Kristiine Ehitus was the leading partner of the consortium. On 23 March 2010, as required by the documents of the public procurement tender, Arco Ehitus OÜ submitted to Järvamaa Education Centre a letter of guarantee of 88,286 euros valid from 23 March 2010 until 31 August 2010.

During construction, it appeared that the documents Järvamaa Education Centre had submitted to the contractor contained a number of deficiencies that were brought to the attention of Järvamaa Education Centre already at the construction meetings. On 24 August 2010, OÜ Kristiine Ehitus notified Järvamaa Education Centre of the fact that if the latter did not discharge its contractual obligations, the Contract would be cancelled on 30 August 2010. Järvamaa Education Centre did not respond by the said date and accordingly the Contract was cancelled.

On 30 August 2010, Järvamaa Education Centre sent Arco Ehitus OÜ and OÜ Kristiine Ehitus a notice of unilateral termination of general renovation contract no 1/344 as of 31 August 2010 and a letter of claim to AS SEB Pank for payment of the guaranteed amount.

On 13 September 2010, Arco Ehitus OÜ and OÜ Kristiine Ehitus filed a statement of claim, seeking recognition of the cancellation of the Contract and the claim for debt. On 27 December 2010, Arco Ehitus OÜ and OÜ Kristiine Ehitus filed additional statements and a specification of the statement of claim according to which their principal claim against the Republic of Estonia amounts to 889,532 euros plus late payment interest. The Republic of Estonia has not admitted the claim and has contested it in full.

The preliminary hearing and hearings in the matter took place at Harju County Court on 17 January 2011 and on 11 April 2011 and 15 June 2011 respectively. The court has not yet ruled on the matter.

The litigation is pending.

Claims of Arco Ehitus OÜ against Plastitehase AS

On 18 December 2007, Arco Ehitus OÜ and Plastitehase AS signed a construction services contract, under which Arco Ehitus OÜ undertook to build an integrated water treatment system for Plastitehase AS. Arco Ehitus OÜ did all of the agreed construction work but Plastitehase AS did not pay for work of 151,170 euros.

Plastitehase AS was declared bankrupt on 1 March 2011 and Ly Mürsoo was appointed the bankruptcy trustee.

On 9 March 2011, Arco Ehitus OÜ filed a proof of claim in which it requested to be transferred the equipment it had installed under the above contract whose title had not transferred to Plastitehase AS, i.e. equipment of 151,170.05 euros. Arco Ehitus OÜ also requested that if the equipment could not be transferred, a corresponding explanation should be provided and its claim against Plastitehase AS should be recognised in the bankruptcy proceedings in an amount of 183,282.75 euros comprising of a principal claim of 151,170.05 euros and late payment interest of 32,112.70 euros.

The creditors' first general meeting was held on 22 March 2011 at Harju County Court.

The bankruptcy proceedings are pending.

Claims of Arco Ehitus OÜ against Wolmreks Ehitus OÜ

On 16 December 2010, Arco Ehitus OÜ, OÜ Wolmreks Ehitus and OÜ Savekate signed an annex to a subcontract by which Arco Ehitus OÜ took over all of the rights and obligations of OÜ Wolmreks Ehitus arising from a subcontract signed between OÜ Wolmreks Ehitus and OÜ Savekate on 25 August 2010. In line with the annex, Arco Ehitus OÜ paid 51,768.44 euros to OÜ Savekate on behalf of OÜ Wolmreks Ehitus and OÜ Wolmreks Ehitus undertook to pay Arco Ehitus OÜ 51,768.44 euros for taking over the obligation by 20 December 2010 at the latest.

On 28 December 2010, Arco Ehitus OÜ, OÜ Wolmreks Ehitus and AS Parmet signed a new annex to the subcontract by which Arco Ehitus OÜ took over all of the rights and obligations of OÜ Wolmreks Ehitus arising from a subcontract signed between OÜ Wolmreks Ehitus and AS Parmet on 16 December 2010. In line with the annex, Arco Ehitus OÜ paid 15,338.80 euros to AS Parmet on behalf of OÜ Wolmreks Ehitus and OÜ Wolmreks Ehitus undertook to pay Arco Ehitus OÜ 15,338.80 euros for taking over the obligation by 31 December 2010 at the latest.

On 6 January 2011, Arco Ehitus OÜ, OÜ Wolmreks Ehitus and engineering bureau Tandem OÜ signed an annex to a design services contract by which Arco Ehitus OÜ took over all of the rights and obligations of OÜ Wolmreks Ehitus arising from a design services contract signed between OÜ Wolmreks Ehitus and engineering bureau Tandem OÜ on 24 May 2010. In line with the annex, Arco Ehitus OÜ paid 3,067.76 euros to engineering bureau Tandem OÜ on behalf of OÜ Wolmreks Ehitus and OÜ Wolmreks Ehitus undertook to pay Arco Ehitus OÜ 3,067.76 euros for taking over the obligation by 10 January 2011 at the latest.

According to the agreements between the parties, OÜ Wolmreks Ehitus undertook to pay Arco Ehitus OÜ a total of 70,175 euros for taking over its obligations. By the date of release of this report, OÜ Wolmreks Ehitus has not fulfilled its obligations.

On 21 February 2011, OÜ Wolmreks Ehitus was declared bankrupt and Indrek Lepsoo was appointed the bankruptcy trustee. On 4 March 2011, Arco Ehitus OÜ filed a proof of claim in which it requested recognition of a claim of 71,092.89 euros.

The creditors' first general meeting was held on 10 March 2011 at Harju County Court.

The bankruptcy proceedings are pending.

Action brought by Arco Ehitus OÜ against Sillamäe City Government and action brought by Sillamäe City Government against Arco Ehitus OÜ

On 6 September 2010, a consortium consisting of OÜ Wolmreks Ehitus, OÜ Kristiine Ehitus and Arco Ehitus OÜ submitted a joint bid in the public procurement tender for the renovation of the building of Sillamäe sport complex Kalev. The bid included the bidders' authorisation document by which OÜ Kristiine Ehitus and Arco Ehitus OÜ authorised member of the management board of OÜ Wolmreks Ehitus Hanno Muga to be the joint bidders' official representative in matters pertaining to the procurement proceedings and conclusion of the public procurement contract.

On 14 October 2010, Sillamäe City Government adopted a resolution in which it declared the joint bid made by OÜ Wolmreks Ehitus, OÜ Kristiine Ehitus and Arco Ehitus OÜ successful.

On 17 December 2010, Sillamäe City Government submitted to Arco Ehitus OÜ a letter for checking the bidder's qualification. Arco Ehitus OÜ responded to the letter on 22 December 2010 with a statement that Arco Ehitus OÜ had given OÜ Wolmreks Ehitus a letter of authorisation that empowered and obligated OÜ Wolmreks Ehitus to conduct all procedures related to the public procurement tender for the renovation of the building of Sillamäe sport complex Kalev. In the letter, Arco Ehitus OÜ did not supply any proof of the powers granted to Adu Haki.

On 28 January 2011, Arco Ehitus OÜ received a letter from Sillamäe City Government together with a resolution of the Sillamäe City Government of 27 January 2011 that: a) invalidated the resolution by which the bid had been declared successful; b) declared the bid offering the second-best price successful; c) claimed compensation of damages from joint bidders OÜ Wolmreks Ehitus, OÜ Kristiine Ehitus and Arco Ehitus OÜ that had withdrawn the bid that had been declared successful. The amount claimed from the bidders as their joint and several liability was the difference between the price of the withdrawn bid and the price of the bid that was declared successful next, i.e. 12,549.21 euros including realisation of the guarantee issued by AS SEB Pank as security of the bid.

On 1 February 2011, Arco Ehitus OÜ submitted an explanation to Sillamäe City Government according to which Arco Ehitus OÜ did not notify the City Government in its letter of 22 December 2010 of its intention to withdraw from the public procurement and that Arco Ehitus OÜ had not authorised anyone to withdraw from the public procurement. In addition, Arco Ehitus OÜ explained that in connection with OÜ Wolmreks Ehitus's liquidation and bankruptcy proceedings the bidder did not meet the qualification requirements at the date the procurement contract was signed and therefore Sillamäe City Government did not have the right to sign a procurement contract.

On 16 February 2011, Sillamäe City Government sent Arco Ehitus OÜ a claim for compensation of damages in which it demanded that Arco Ehitus OÜ transfer compensation of 4,879.81 euros to the current account of Sillamäe City Government by 25 February 2011 at the latest.

On 27 February 2011, Arco Ehitus OÜ filed a complaint with Tartu Administrative Court in which it requested that the resolution of Sillamäe City Government of 27 January 2011 be declared invalid. Tartu Administrative Court issued a ruling on 4 March 2011 by which it returned the complaint because the mandatory legal procedure for preliminary out-of-court settlement of the matter had not been observed.

Arco Ehitus OÜ did not agree with the ruling of Tartu Administrative Court and found that this was not lawful or justified. Accordingly, on 17 March 2011 Arco Ehitus OÜ lodged an appeal against the ruling with Tartu Administrative Court requesting that the ruling be declared invalid. The appeal has not yet been ruled on.

On 28 March 2011, Arco Ehitus OÜ received a court ruling from Viru County Court together with a statement of claim filed by the City of Sillamäe and an order to respond to the statement of claim. Arco Ehitus OÜ does not admit the claim for compensation submitted by the City of Sillamäe and lodged a response to the statement of claim. Arco Ehitus OÜ is of the opinion that the City of Sillamäe has no basis for claiming compensation of damages from Arco Ehitus OÜ. On the contrary, the City of Sillamäe has the obligation to return to Arco Ehitus OÜ the gain derived on unjust bases from the realisation of the letter of guarantee of 7,669.40 euros.

On 8 June 2011, the bankruptcy trustee of OÜ Kristiine Ehitus (bankrupt since 23 May 2011) Peeter Sepper filed an application for dismissal of the action. Arco Ehitus OÜ and the City of Sillamäe presented their positions on 27 June 2011 and 17 June 2011 respectively. On 13 July 2011 the court ruled that the action brought by the City of Sillamäe against OÜ Kristiine Ehitus for compensation of damages should be dismissed.

A hearing in the above matter will take place at Viru County Court on 20 September 2011.

The litigation is pending.

Claims of Arco Ehitus OÜ against Kristiine Ehitus OÜ

On 31 March 2010, Arco Ehitus OÜ and OÜ Kristiine Ehitus signed a subcontract for construction services by which Arco Ehitus OÜ undertook to build the Estonian Aviation Academy building and OÜ Kristiine Ehitus undertook to pay for the construction work as stated in signed and submitted delivery documents. Arco Ehitus OÜ performed the work as agreed in the contract and submitted records of delivery as well as associated invoices. OÜ Kristiine Ehitus did not pay Arco Ehitus OÜ for work of 29,551.75 euros.

On 22 December 2010, Arco Ehitus OÜ, OÜ Kristiine Ehitus and JD Options OÜ signed an annex to the subcontract under which Arco Ehitus OÜ took over all of the rights and obligations of OÜ Kristiine Ehitus arising from a subcontract signed between OÜ Kristiine Ehitus and JD Options OÜ. Arco Ehitus OÜ paid JD Options OÜ 3,719.23 euros on behalf of OÜ Kristiine Ehitus and OÜ Kristiine Ehitus undertook to pay Arco Ehitus OÜ 3,719.23 euros for taking over the obligation by 30 December 2010 at the latest.

On 18 February 2011, Arco Ehitus OÜ and OÜ Kristiine Ehitus signed a loan agreement under which Arco Ehitus OÜ gave OÜ Kristiine Ehitus a loan of 3,601.68 euros for discharging the tax commitments of OÜ Kristiine Ehitus. OÜ Kristiine Ehitus undertook to repay the loan principal with accrued interest by 19 April 2011 at the latest. The obligation was not discharged in line with the agreement nor has it been discharged to date.

On 23 May 2011, OÜ Kristiine Ehitus was declared bankrupt and Peeter Sepper was appointed the bankruptcy trustee. On 13 June 2011, Arco Ehitus OÜ submitted a proof of claim in which it requested that its claim of 79,678.18 euros should be recognised in full.

The creditors' first general meeting took place at Harju County Court on 16 June 2011.

The bankruptcy proceedings are pending.

Claims of Arco Ehitus OÜ against AS K&H

On 3 December 2008, AS K&H and Arco Ehitus OÜ signed a contract under which Arco Ehitus OÜ undertook to perform the water management project for the catchment area of the Emajõe and Võhandu rivers, Emajõe subproject; design and build of drinking water facilities (the Emajõe contract). Arco Ehitus OÜ performed the work as agreed in the Emajõe contract and submitted invoices to AS K&H. In line with the contract, AS K&H withheld 5% of each invoice as warranty retention. Altogether, 277,307.90 euros could be withheld based on the Emajõe contract and associated invoices until the date of issuance of a letter of guarantee.

On 28 October 2010, AS K&H and Arco Ehitus OÜ signed an agreement whereby AS K&H undertook to waive the demand for a bank letter of guarantee stipulated in the Emajõe contract, to accept an Arco Vara AS letter of guarantee as security for the performance of the obligations of Arco Ehitus OÜ and to pay Arco Ehitus OÜ the amount retained on the basis of the Emajõe contract when a letter of guarantee is issued by Arco Vara AS.

On 28 October 2010, Arco Ehitus OÜ and AS K&H signed a construction services contract for a water management project for the wastewater collection area of Tamsalu (the Tamsalu contract). AS K&H waived the demand for a bank letter of guarantee and accepted an Arco Vara AS letter of guarantee as security for the performance of the obligations of Arco Ehitus OÜ.

On 5 April 2011, AS K&H signed a real right contract by which it mortgaged some of its properties under a combined mortgage of 1,000,000 euros to Arco Ehitus OÜ.

On 30 May 2011, Arco Ehitus OÜ sent AS K&H a proof of claim in which it demanded settlement of a claim of 296,087.11 arising from the Emajõe contract and settlement of a claim of 569,533.86 euros arising from the Tamsalu contract, i.e. 865,620.97 euros in aggregate.

On 3 June 2011, Arco Ehitus OÜ and AS K&H signed a compromise agreement in which AS K&H accepted the claim arising from the Emajõe contract in an amount of 289,267.81 euros and the claim arising from the Tamsalu contract in an amount of 423,941.99 euros. The parties also agreed that the above claims constitute the entire claim and that Arco Ehitus OÜ has no other claims against AS K&H in connection with the Emajõe contract and that the claims will fall due as of the signature of the compromise agreement. Under an agreement on the discharge and transfer of claim, AS K&H Arco transferred to Ehitus OÜ a claim of 200,995.16 euros and associated collateral claims against AS Tamsalu Vesi. Under the compromise agreement, Arco Ehitus OÜ transferred the combined mortgage to the extent of 350,000 euros

free of charge to law office Varul AS. Thus, since 3 June 2011, the value of the combined mortgage created for the benefit of Arco Ehitus OÜ is 650,000 euros.

On 18 July 2011, Tartu County Court declared AS K&H bankrupt and appointed Sirje Tael to act as the bankruptcy trustee.

On 15 August 2011, Arco Ehitus OÜ submitted a statement of claim to the bankruptcy trustee in which it requested that the claim of Arco Ehitus OÜ should be recognised in the bankruptcy proceedings in an amount of 512,214.64 euros.

The creditors' first general meeting will take place at Tartu County Court on 22 August 2011.

The bankruptcy proceedings are pending.

15. Events after the reporting period

Arco Ehitus OÜ cancels a contract with Estonian University of Life Sciences

On 14 July 2010, a consortium consisting of Arco Ehitus OÜ, OÜ Wolmreks Ehitus and OÜ Kristiine Ehitus signed a general contract for construction services with the Estonian University of Life Sciences. The authorised representative of the consortium was OÜ Wolmreks Ehitus that had been assigned the responsibility of performing the entire construction work with the agreement of the consortium. In November 2010, it became apparent that OÜ Wolmreks Ehitus and OÜ Kristiine Ehitus were in financial difficulty and on most projects work had been suspended or had been performed to a minimal extent. In addition, it became apparent that the construction work for the Estonian University of Life Sciences had not been performed in line with the agreed dates and that the builder was behind the agreed construction schedule. Arco Ehitus OÜ immediately began seeking solutions and for more effective and efficient performance of the contract it was considered necessary to change the lead partner of the consortium. As from 1 December 2010, the lead partner and authorised representative of the consortium is Arco Ehitus OÜ.

On 21 February 2011, OÜ Wolmreks Ehitus was declared bankrupt and Arco Ehitus OÜ became solely responsible for the performance of the contract.

The price calculations for the contract with the Estonian University of Life Sciences were prepared by OÜ Wolmreks Ehitus. Since the preparation of the bid, the prices of construction services have risen by around 30-40% and the new calculations prepared by Arco Ehitus OÜ indicate that the cost of the contract will prove 447,000 larger than initially estimated. The Estonian University of Life Sciences refused to compensate the increase in the cost of the contract. Continuing construction under the original terms and conditions and without amending the contract would have had a highly adverse financial impact on Arco Ehitus OÜ.

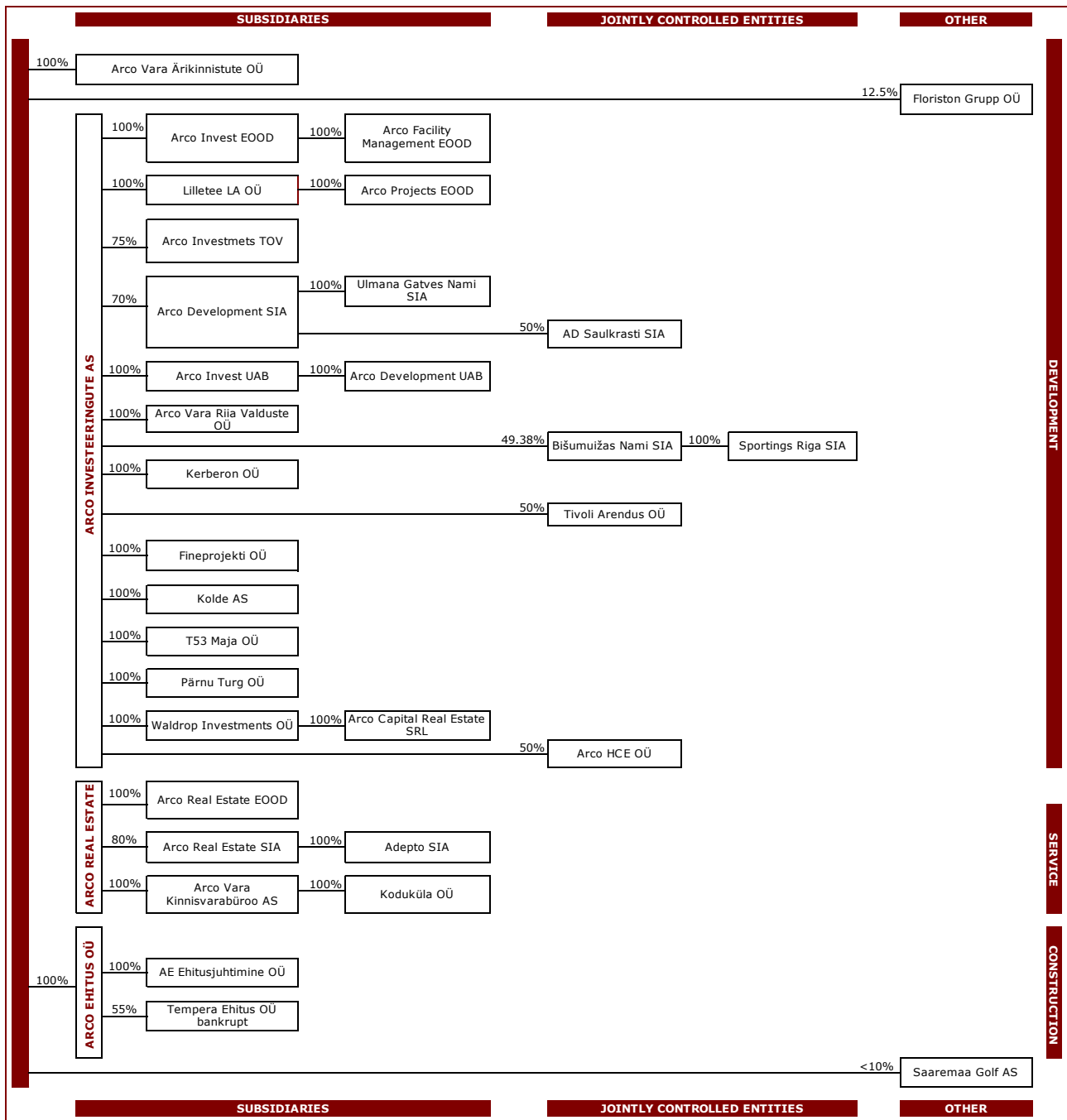
On 11 July 2011, Arco Ehitus OÜ sent the Estonian University of Life Sciences a notice of cancellation of contract and a proposal for signing a final statement of work completed.

On 22 July 2011, the Estonian University of Life Sciences sent its response to the notice of cancellation in which it took the position that the notice of cancellation sent by Arco Ehitus OÜ was void and that the Estonian University of Life Sciences itself will cancel the general contract for construction services.

The notice of cancellation sent by Arco Ehitus OÜ and the cancellation of contract were completely lawful and there were no legal or contractual impediments to cancelling the contract. Thus, the general contract for construction services has been cancelled by Arco Ehitus OÜ as of 12 July 2011 and it is not legally possible to cancel a contract already cancelled by Arco Ehitus OÜ.

16. Structure of Arco Vara Group

As at 30 June 2011



Statement by the management board

The management board of Arco Vara AS has prepared the interim report for the second quarter and first six months of 2011 as set out on pages 2-34.

The interim report has been prepared in accordance with International Financial Reporting Standards (IFRS) and it gives a true and fair view of the financial position, financial performance and cash flows of Arco Vara AS. Arco Vara AS is a going concern.



Lembit Tampere
Chief Executive Officer and Member of the Management Board

26 August 2011