

SAF Tehnika A/S

**Consolidated Annual Accounts
for the year ended 30 June 2005**

**SAF TEHNIKA A/S
CONSOLIDATED ANNUAL ACCOUNTS
FOR THE YEAR ENDED 30 JUNE 2005**

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Report of the Board

Description of activities

SAF Tehnika (hereafter – the Group) is a manufacturer, producer and distributor of digital microwave point-to-point radio data transmission equipment which is mainly used by telecommunication operators to provide voice and data transmission as an alternative to cable channels. The Group markets its portfolio of approximately 130 products to cellular network operators, data service providers (such as internet service providers and telecommunication companies), governments and private companies. The purpose of the Group is to provide wireless connections for data and voice transmission for acceptable price. The Group attributes its success to its flexibility, its distinctive approach to research and development and its ability to deliver high value solutions to its customers at a very competitive price.

Group activities during the financial year

The Group's consolidated net sales for 12 month period of financial year 2004/2005 were Ls 11 066 391. Despite the revenues from China decreased by approximately Ls 6 000 000 (in the previous financial year China represented 57% of revenues), turnover constituted 86% of the previous financial year's consolidated net sales. Sales to Asia, Africa and Latin America increased rapidly. Over the past 12 months the Group has entered 15 new markets, thereby increasing the total number of active markets by 50% (now 45 countries). Nearly all of the new countries are considered to be emerging markets.

The consolidated net profit of the Group for financial year 2004/2005 (incorporating SAF Tehnika Sweden) was Ls 1 559 327. Net profit compared with the previous year was affected mainly by decreased turnover (less beneficial economies of scale) and SAF Tehnika Sweden costs. Ongoing developments such as the new common modem project are being undertaken in order to address this issue. The key determinant for better profitability measures solely rests on increased turnover due to absolute fixed cost levels.

During the reporting year the Group increased production capacity by investing Ls 587 143 into property, plant and equipment and intangible assets and recruiting 20 new employees.

The Group signed contracts with all of Sweden's Tele2 subsidiaries in Russia. Furthermore SAF Tehnika has become an official supplier for Russia's second-largest mobile network operator VimpelCom. Also the sale of SAF network management system has been introduced.

In addition to participating in the CommunicAsia 2005 (Singapore) and CeBit (Hanover) exhibitions, the Group also became a member of the Latvian Chamber of Commerce and Industry. The combined effects of the above activities are expected to result in new collaboration partners and clients.

The Group is planning to expand further internationally by penetrating new geographic markets both in developing and developed countries while accommodating local user preferences and market-specific characteristics.

Following the majority shareholder decision taken at the previous annual general meeting, the Group paid a Ls 1 per share dividend and implemented a 2 for 1 bonus share issue.

Scientific research and development

The Company has an ongoing focus towards the development of new products as well as the improvement of existing ones, thereby constantly offering more qualitative and diverse solutions. For example, the Group has completed the indoor unit (IDU) and outdoor unit (ODU) testing process by implementation of IDU thermo-testing.

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Report of the Board (continued)

Foreign branch offices


Estonian subsidiary SAF International was liquidated during the previous financial year in order to streamline operations, while Swedish subsidiary SAF Tehnika Sweden worked on a project related to the launch of a CFQ system.

Court proceedings

Following an audit of the SAF Tehnika A/s (Company) by the the Latvian State Revenue Service (SRS), the SRS deemed that the Company was obliged to pay additional income tax (and a penalty). The Company disagreed with this position and this was therefore contested in the Administrative District Court. The Court satisfied the claim and established that the disputed decision was unfounded and had to be withdrawn. The court decision was not appealed by the SRS and therefore came into force.

Future perspectives

Based on ongoing investments (including increased production capacity) and existing demand levels, management of SAF Tehnika considers that the results of financial year 2005/2006 will be better thanks to the successful income diversification measures undertaken following the unexpected (3G-related) industry slowdown in the Chinese market.



Normunds Bergs
Chairman of the Board

Riga, 4 October 2005

The General Shareholders' Meeting approved the annual report on _____. _____ 2005

Chairman of the General Shareholders' Meeting _____

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STATEMENT OF THE BOARD'S RESPONSIBILITY

The Board of SAF Tehnika A/S (the Company) is responsible for the preparation of the consolidated financial statements of the Company and its subsidiary (the Group).

The consolidated financial statements on pages 7 to 31 are prepared in accordance with the source documents and present fairly the financial position of the Group as of 30 June 2005 and the results of its operations and cash flows for the year ended 30 June 2005.

The above mentioned consolidated financial statements are prepared in accordance with International Financial Reporting Standards on a going concern basis. Appropriate accounting policies have been applied on a consistent basis. Prudent and reasonable judgments and estimates have been made by the Board in the preparation of the consolidated financial statements.

The Board of SAF Tehnika A/S is responsible for the maintenance of proper accounting records, the safeguarding of the Group's assets and the prevention and detection of fraud and other irregularities in the Group. The Board is also responsible for operating the Group companies in compliance with the legislation of their domicile countries (Latvia and Sweden).

On behalf of the Board,

Normunds Bergs
Chairman of the Board



4 October 2005

AUDITORS' REPORT


To the shareholders of SAF Tehnika A/S

We have audited the consolidated financial statements of SAF Tehnika A/S and its subsidiary SAF Tehnika Sweden AB (the "Group") for the year ended 30 June 2005 set out on pages 7 to 31. The audited consolidated financial statements include the consolidated balance sheet as of 30 June 2005 and the related consolidated statements of income, changes in equity and cash flows for the year then ended 30 June 2005 and note disclosure. These consolidated financial statements are the responsibility of SAF Tehnika A/S management, as referred to on page 5. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with International Standards on Auditing issued by International Federation of Accountants. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We read the management report set out on pages 3 to 4 and did not identify material inconsistencies with the audited consolidated financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements give a true and fair view of the financial position of the Group as of 30 June 2005, and of the results of its operations and its cash flows for the year ended 30 June 2005 in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers SIA
Audit company licence No. 5



Juris Lapshe
Certified auditor
Certificate No. 116

Member of the Board

11 October 2005

SAF TEHNIKA A/S
CONSOLIDATED FINANCIAL STATEMENTS
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Consolidated balance sheet

	Note	As at 30 June	
		2005 Ls	2004 Ls
ASSETS			
Non-current assets			
Property, plant and equipment	9	1 045 003	1 042 174
Intangible assets	10	694 396	648 947
Available for sale financial assets		-	31 654
		1 739 399	1 722 775
Current assets			
Inventories	13	4 365 782	2 936 976
Current income tax		181 994	-
Trade and other receivables	12	1 878 465	3 007 072
Derivative financial instruments	11	-	4 446
Cash and cash equivalents	14	105 190	852 257
		6 531 431	6 800 751
Total assets		8 270 830	8 523 526
EQUITY			
Share capital	15	4 974 384	2 995 259
Reserves		1 023 402	10 311
Currency translation reserve		(1 090)	(2 272)
Retained earnings		1 496 625	3 920 569
Total equity		7 493 321	6 923 867
LIABILITIES			
Non-current liabilities			
Deferred tax liabilities	18	15 082	29 422
		15 082	29 422
Current liabilities			
Trade and other payables	16	747 338	919 244
Current income tax liabilities		-	648 006
Borrowings	17	6 101	2 519
Derivative financial instruments	11	8 988	468
		762 427	1 570 237
Total liabilities		777 509	1 599 659
Total equity and liabilities		8 270 830	8 523 526

The notes on pages 11 to 31 are an integral part of these consolidated financial statements.

The consolidated financial statements on pages 7 to 31 were approved by the Board and were signed on its behalf by:

Normunds Bergs
Chairman of the Board

30 September 2005



SAF TEHNIKA A/S
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Consolidated income statement

	Note	Year ended 30 June	
		2005 Ls	2004 Ls
Sales	5	11 066 391	12 818 452
Cost of goods sold	6	(7 144 459)	(6 382 529)
Gross profit		3 921 932	6 435 923
Selling and marketing costs	7	(899 064)	(959 486)
Administrative expenses	8	(1 041 119)	(416 123)
Operating profit		1 981 749	5 060 314
Finance costs – net	19	(37 140)	(252 022)
Profit before income tax		1 944 609	4 808 292
Income tax expense	20	(385 282)	(887 723)
Profit for the year		1 559 327	3 920 569
Attributable to:			
Equity holders of the Company		1 559 327	3 920 569
		<u>1 559 327</u>	<u>3 920 569</u>
Earnings per share for profit attributable to the equity holders of the Company during the year (expressed in Ls per share)			
– basic	21	0.52	1.32
– diluted	21	0.52	1.32

The notes on pages 11 to 31 are an integral part of these consolidated financial statements.

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Consolidated statement of changes in equity

	Share capital	Share premium	Reserves*	Currency translation reserve	Retained earnings	Total
	Ls	Ls	Ls	Ls	Ls	Ls
Balance at 30 June 2003	200 303	521 679	70 645	-	811 786	1 604 413
Issue of share capital	67 637	1 531 649	-	-	-	1 599 286
Costs of issue of capital	-	(48 129)	-	-	-	(48 129)
Dividend relating to 2002/2003	-	-	-	-	(150 000)	(150 000)
Allocation of profit	-	-	661 786	-	(661 786)	-
Issue of share capital	722 120	-	(722 120)	-	-	-
Currency translation differences	-	-	-	(2 272)	-	(2 272)
Profit for the year	-	-	-	-	3 920 569	3 920 569
Balance at 30 June 2004	990 060	2 005 199	10 311	(2 272)	3 920 569	6 923 867
Issue of share capital	1 980 120	-	-	-	(1 980 120)	-
Costs of issue of capital	-	(995)	-	-	-	(995)
Dividend relating to 2003/2004	-	-	-	-	(990 060)	(990 060)
Allocation of profit	-	-	1 013 091	-	(1 013 091)	-
Currency translation differences	-	-	-	1 182	-	1 182
Profit for the year	-	-	-	-	1 559 327	1 559 327
Balance at 30 June 2005	2 970 180	2 004 204	1 023 402	(1 090)	1 496 625	7 493 321

* Reserves have been created by allocation of profit in accordance with the shareholders' decision and can be distributed subject to shareholders' approval.

The notes on pages 11 to 31 are an integral part of these consolidated financial statements.

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Consolidated cash flow statement

	Note	Year ended 30 June	
		2005 Ls	2004 Ls
Cash flows from operating activities			
Cash generated from operations	23	1 833 090	2 073 282
Interest paid		(27 562)	(111 381)
Income tax paid		(995 202)	(241 548)
Net cash generated from operating activities		810 326	1 720 353
Cash flows from investing activities			
Business acquisition		-	(636 525)
Received as a result of subsidiary liquidation		27 447	-
Purchases of property, plant and equipment (PPE)		(461 411)	(468 224)
Proceeds from sale of PPE		184	3 571
Purchases of intangible assets		(126 500)	(122 269)
Interest received		2 986	7 132
Net cash used in investing activities		(557 294)	(1 216 315)
Cash flows from financing activities			
Proceeds from issuance of ordinary shares		-	1 551 157
Finance lease payments		-	(280 803)
Proceeds from borrowings		3 582	-
Repayments of borrowings		-	(773 675)
Dividends paid to Company's shareholders		(990 060)	(150 000)
Net cash (used in) / from financing activities		(986 478)	346 679
Effects of exchange rate changes		(13 621)	-
Net (decrease) / increase in cash and cash equivalents		(747 067)	850 717
Cash and cash equivalents at the beginning of the year		852 257	1 540
Cash and cash equivalents at the end of the year	14	105 190	852 257

The notes on pages 11 to 31 are an integral part of these consolidated financial statements.

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Notes to the consolidated financial statements

1. General information

SAF Tehnika (the Company) and its subsidiary (together the Group) is a designer, producer and distributor of digital microwave point-to-point radio data transmission equipment which offers an alternative to cable channels. The Group markets its portfolio of approximately 130 products to cellular network operators, data service providers (such as internet service providers and telecommunication companies), governments and private companies. The Company owns 100% of a subsidiary company SAF Tehnika Sweden AB, a research and development company of microwave radio equipment, which was established in May 2004.

The Company is a public joint stock company incorporated under the laws of the Republic of Latvia. The address of its registered office is Ganību Dambis 24a, Riga, Latvia.

The shares of the Company are listed on Riga Stock Exchange, Latvia.

These consolidated financial statements have been approved for issue by the Board of Directors on 4 October 2005.

The Company's management does not have the power to amend the consolidated financial statements after issue.

The annual full reporting period for the Group is set from July 1 through June 30.

2. Summary of significant accounting policies

The principal accounting policies adopted in the preparation of these consolidated financial statements are set out below.

A Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS). The consolidated financial statements have been prepared under the historical cost convention as modified by the revaluation of certain financial assets (including derivative financial instruments).

The preparation of financial statements in conformity with IFRS requires the use of estimates and assumptions. Areas including significant judgements or complexity, or areas with estimates and judgements significant for preparation of financial statements are disclosed in Note 4 and Note 10.

The accounting policies used by the Group are consistent with those used in the previous accounting period.

Early adoption of standards

In 2003/2004 the Group early adopted the IFRS below, which are relevant to its operations.

IAS 1	(revised 2003)	Presentation of Financial Statements
IAS 2	(revised 2003)	Inventories
IAS 8	(revised 2003)	Accounting Policies, Changes in Accounting Estimates and Errors
IAS 10	(revised 2003)	Events after the Balance Sheet Date
IAS 16	(revised 2003)	Property, Plant and Equipment
IAS 17	(revised 2003)	Leases
IAS 21	(revised 2003)	The Effects of Changes in Foreign Exchange Rates

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Notes to the consolidated financial statements (continued)

2. Summary of significant accounting policies (continued)

A Basis of preparation (continued)

IAS 24	(revised 2003)	Related Party Disclosures
IAS 27	(revised 2003)	Consolidated and Separate Financial Statements
IAS 32	(revised 2003)	Financial Instruments: Disclosure and Presentation
IAS 33	(revised 2003)	Earnings per Share
IAS 39	(revised 2003)	Financial Instruments: Recognition and Measurement
IAS 36	(revised 2003)	Impairment of Assets
IAS 38	(revised 2003)	Intangible Assets

B Consolidation and business combinations

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group's Parent company controls another entity.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases. Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

The Group uses the purchase method of accounting to account for the acquisition of subsidiaries or businesses.

The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill.

C Foreign currency translation

(a) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in Lats (Ls), which is the Company's functional and presentation currency.

(b) Transactions and balances

Foreign currency transactions are translated into the presentation currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

(c) Group companies

The results and financial position of all the Group entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

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Notes to the consolidated financial statements (continued)

2. Summary of significant accounting policies (continued)

C Foreign currency translation (continued)

- (i) assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- (ii) income and expenses for each income statement are translated at average exchange rates (unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the dates of the transactions); and
- (iii) all resulting exchange differences are recognised as a separate component of equity.

Goodwill and fair value adjustments arising on the acquisition of a foreign entity or business are treated as assets and liabilities of the foreign entity and translated at the closing rate.

D Property, plant and equipment

Property, plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably.

All other repairs and maintenance are charged to the income statement during the financial period in which they are incurred.

Depreciation on assets is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives, as follows:

	% per annum
Mobile phones	50
Technological equipment	33.33
Motor vehicles	20
Other fixtures and fittings	25

Leasehold improvements are amortized on a straight-line basis over the shorter of the estimated useful life of leasehold improvement and the term of lease.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note G).

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement.

E Intangible assets

(a) Intangible assets arising from development

Intangible assets arising from development are recorded at cost less accumulated amortisation. Cost of intangible assets acquired in a business combination is their fair value at the acquisition date.

The Group has not incurred development expenditure qualifying for capitalisation. Product prototypes have been acquired in business combination. Amortisation is charged from the moment when the underlying assets start generating cash flows. The amortisation is calculated using the straight line method to allocate the cost of product prototypes over the estimated useful life of 10 years.

Notes to the consolidated financial statements (continued)

2. Summary of significant accounting policies (continued)

E Intangible assets (continued)

(b) Trademarks and licences

Trademarks and licences are shown at historical cost. Trademarks and licences have a definite useful life and are carried at cost less accumulated amortisation. Amortisation is calculated using the straight-line method to allocate the cost of trademarks and licences over their estimated useful lives of usually three years.

(c) Computer software

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised over their estimated useful lives of three years.

Costs associated with developing or maintaining computer software programmes are recognized as an expense as incurred.

F Research and development

Research expenditure is recognised as an expense as incurred. The Group has not incurred development expenditure qualifying for capitalization, except for assets acquired in a business combination as described in Note E (a).

G Impairment of assets

Assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units).

H Segment reporting

A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of components operating in other economic environments. A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments.

I Inventories

Inventories are stated at the lower of cost and net realisable value. Cost is determined using the first-in, first-out (FIFO) method. Finished goods and work in progress are stated at material cost. Labour costs and overheads are not material to the financial statements. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

J Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of receivables. The amount of the provision is the difference between the carrying amount and the recoverable amount. The amount of changes in provision is recognised in the income statement.

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Notes to the consolidated financial statements (continued)

2. Summary of significant accounting policies (continued)

K Cash and cash equivalents

Cash and cash equivalents include bank account balances, time deposits with banks and other short-term highly liquid investments with original maturities of three months or less.

L Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are charged against the share premium account. Incremental costs directly attributable to the acquisition of a business are included in the cost of acquisition as part of the purchase consideration.

M Borrowings

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the income statement over the period of the borrowings using the effective interest rate method. Borrowings are classified as current liabilities unless the Group has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

N Deferred income tax

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, if the deferred income tax arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss, it is not accounted for. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

O Employee benefits

The Group makes social insurance contributions to the State's health, retirement benefit and unemployment schemes at the statutory rates in force during the year, based on gross salary payments. The Group pays fixed contributions to privately administered pension insurance plan. The Group will have no legal or constructive obligations to pay further contributions if the fund or pension plan do not hold sufficient assets to pay all employee benefits relating to employee service in the current and prior periods. The cost of these payments is included into the income statement in the same period as the related salary cost.

P Revenue recognition

Revenue comprises the fair value for the sale of goods and services, net of value-added tax, rebates and discounts and after eliminated sales within the Group. Revenue is recognised as follows:

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Notes to the consolidated financial statements (continued)

2. Summary of significant accounting policies (continued)

P Revenue recognition (continued)

(a) *Sales of goods*

Sales of goods are recognised when a Group entity has delivered products to the customer and the customer has accepted the products in accordance with the contract terms, and collectibility of the related receivables is reasonably assured.

(b) *Sales of services*

Sales of services are recognised in the accounting period in which the services are rendered.

R Leases

Leases of property, plant and equipment in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

S Dividend distribution

Dividend distribution to the Company's shareholders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved by the Company's shareholders.

T New accounting standards and IFRIC interpretations

Certain new accounting standards and IFRIC interpretations have been published that are mandatory for accounting periods beginning on or after 1 December 2005. The Group's assessment of the impact of these new standards and interpretations is set out below.

(a) *IFRS 6, Exploration and Evaluation of Mineral Resources*

The Group does not have any Mineral Resources assets. This standard will not affect the Group's financial statements.

(b) *IFRIC 3, Emission Rights*

The Group does not participate in an emission rights scheme. This interpretation will not affect the Group's financial statements.

(c) *IFRIC 4, Determining whether an Asset Contains a Lease*

The Group does not have assets containing a lease. This interpretation will not affect the Group's financial statements.

(d) *IFRIC 5, Rights to Interests arising from Decommissioning, Restoration and Environmental Rehabilitation Funds*

The Group does not have interests in decommissioning, restoration and environmental rehabilitation funds. This interpretation will not affect the Group's financial statements.

(e) *IFRIC 6, Liabilities arising from Participating in a Specific Market — Waste Electrical and Electronic Equipment*

The Group does not produce or sell electrical and electronic equipment supplied to private households. This interpretation will not affect the Group's financial statements.

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Notes to the consolidated financial statements (continued)

3. Financial risk management

(1) Financial risk factors

The Group's activities expose it to a variety of financial risks:

- (a) foreign exchange risk,
- (b) credit risk,
- (c) liquidity risk,
- (d) cash flow and interest-rate risk.

The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance. The Group uses derivative financial instruments to hedge certain risk exposures.

Risk management is carried out by the Finance Department. Finance Department identifies, evaluates and hedges financial risks in close co-operation with other Group's operating units.

(a) Foreign exchange risk

The Group operates internationally and is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the US dollar.

Foreign exchange risk arises primarily from future commercial transactions, recognised assets and liabilities. To manage their foreign exchange risk arising from future commercial transactions, recognised assets and liabilities, the Group use forward contracts. Foreign exchange risk arises when future commercial transactions, recognised assets and liabilities are denominated in a currency that is not the entity's functional currency. Finance Department is responsible for managing the net position in each foreign currency by using external forward currency contracts.

The Group's risk management policy is to hedge between 65% and 85% of anticipated transactions (mainly export sales) in US dollar for the subsequent 6 months.

(b) Credit risk

From time to time the Group has significant concentrations of credit risk in connection to its overseas customers. The Group has policies in place to ensure that wholesale sales of products are made to customers with an appropriate credit history. If customers are located in countries with high credit risk, then Letters of Credit issued by reputable credit institutions are used as credit risk management tool. In situations where no Letters of Credit can be obtained from a reputable credit institutions prepayments are requested from the customers.

(c) Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and the availability of funding through the availability of short term borrowings secured by receivables under the Letters of Credit terms. Due to the dynamic nature of the underlying businesses, Finance Department aims to maintain flexibility in funding by keeping credit lines available.

(d) Cash flow and interest rate risk

As the Group does not have significant interest bearing assets or liabilities, the Group's income and cash flows are substantially independent of changes in market interest rates.

(2) Accounting for derivative financial instruments and hedging activities

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value at the balance sheet date. All changes in fair value of the hedge instruments are recognized in income statement.

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3. Financial risk management (continued)

(3) Fair value estimation

The fair value of forward foreign exchange contracts is determined using forward exchange market rates at the balance sheet date.

The nominal value less estimated credit adjustments of trade receivables and payables are assumed to approximate their fair values.

4. Critical accounting estimates and judgements

Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results.

Fair value of Product prototypes

The Group has acquired intangible assets Product prototypes in a business combination as described in Note 10 and Note 24. The fair value of those assets was determined based on a number of assumptions and estimates as described in Note 10.

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5. Segment information and sales

The Group operates in a single business and geographical segment. Under IAS 14 geographical segment is determined by a reference to the dominant source of geographical risks which is the location of its main production unit in Latvia.

The information on sales by regions is presented below for information purposes only and should not be considered as segmental information as defined by IAS 14.

	Year ended 30.06.2005	Year ended 30.06.2004
	Ls	Ls
Asia	1 444 883	7 415 401
America	1 541 739	107 086
Africa	337 489	29 582
Europe	4 050 679	4 234 147
CIS	2 646 720	1 032 236
Middle East	1 044 881	-
	11 066 391	12 818 452

6. Cost of goods sold

	Year ended 30.06.2005	Year ended 30.06.2004
	Ls	Ls
Purchases and subcontractors	5 046 566	5 190 051
Inventory impairment	135 030	73 676
Salary expenses (incl. accruals for unused annual leave)	943 669	521 317
Social insurance (incl. accruals for unused annual leave)	252 715	123 451
Depreciation and amortization	378 900	228 096
Delivery expenses	74 692	55 490
Lease of premises	86 088	100 396
Low value inventory	13 489	14 842
Public utilities costs	34 915	20 496
Transportation costs	17 510	12 780
Other production costs	160 885	41 934
	7 144 459	6 382 529

Purchases and subcontractors cost includes research expense of Ls 13 767 (2003/2004: Ls 16 487).

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7. Selling and marketing costs

	Year ended 30.06.2005 Ls	Year ended 30.06.2004 Ls
Advertising and marketing costs	335 095	632 907
Salary expenses (incl. accruals for unused annual leave)	232 839	131 398
Social insurance (incl. accruals for unused annual leave)	58 089	31 970
Business trip expenses	104 428	71 326
Depreciation and amortization	105 182	59 542
Other selling and distribution expenses	63 431	32 343
	899 064	959 486

8. Administrative expenses

	Year ended 30.06.2005 Ls	Year ended 30.06.2004 Ls
Salary expenses (incl. accruals for unused annual leave)	256 284	102 129
Social insurance (incl. accruals for unused annual leave)	67 536	23 153
Depreciation and amortization	69 358	45 734
Provisions for bad and doubtful accounts receivable	266 592	(20 257)
Bank commissions	24 565	27 846
Office expenses	10 321	11 154
IT services	26 314	11 718
Communication expenses	44 775	14 634
Representation costs	29 656	14 543
Business trip expenses	20 300	22 307
Sponsorship	44 521	55 200
Other administrative expenses	180 897	107 962
	1 041 119	416 123

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Notes to the consolidated financial statements (continued)

9. Property, plant and equipment

	Leasehold improvements	Equipment and machinery	Other assets	Advances for assets	Total
	Ls	Ls	Ls	Ls	Ls
Year ended 30 June 2004					
Opening net book amount	37 456	328 255	130 020	12 563	508 294
Additions	177 135	265 024	108 618	24 312	575 089
Business acquisition	-	225 606	3 880	-	229 486
Reclassified	-	11 179	1 384	(12 563)	-
Disposals at cost	-	(2 779)	-	-	(2 779)
Depreciation charge	(22 524)	(202 117)	(44 614)	-	(269 255)
Depreciation of disposed assets	-	1 339	-	-	1 339
Closing net book amount	192 067	626 507	199 288	24 312	1 042 174
Year ended 30 June 2005					
Opening net book amount	192 067	626 507	199 288	24 312	1 042 174
Additions	107 766	318 988	33 697	192	460 643
Reclassified	3 200	21 112	-	(24 312)	-
Disposals at cost	-	(1 841)	-	-	(1 841)
Depreciation charge	(44 353)	(343 995)	(69 238)	-	(457 586)
Depreciation of disposed assets	-	1 613	-	-	1 613
Closing net book amount	258 680	622 384	163 747	192	1 045 003
At 30 June 2003					
Cost	42 925	508 035	147 551	12 563	711 074
Accumulated depreciation	(5 469)	(179 780)	(17 531)	-	(202 780)
Net book amount	37 456	328 255	130 020	12 563	508 294
At 30 June 2004					
Cost	220 060	1 007 065	261 433	24 312	1 512 870
Accumulated depreciation	(27 993)	(380 558)	(62 145)	-	(470 696)
Net book amount	192 067	626 507	199 288	24 312	1 042 174
At 30 June 2005					
Cost	331 026	1 345 324	295 130	192	1 971 672
Accumulated depreciation	(72 346)	(722 940)	(131 383)	-	(926 669)
Net book amount	258 680	622 384	163 747	192	1 045 003

During the reporting year the Group has not concluded operating or finance lease agreements.

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10. Intangible assets

	Goodwill	Product prototypes	Trademarks & licenses	Software	Advances	Total
	Ls	Ls	Ls	Ls	Ls	Ls
Year ended 30 June 2004						
Opening net book amount	-	-	51 324	19 981	10 764	82 069
Additions	-	-	36 580	73 417	12 272	122 269
Business acquisition	511 051	-	-	-	-	511 051
Reclassified	-	-	10 764	-	(10 764)	-
Disposals	-	-	(2 325)	-	-	(2 325)
Amortization charge	-	-	(38 191)	(25 926)	-	(64 117)
Closing net book amount	511 051	-	58 152	67 472	12 272	648 947
Adjustment*	(511 051)	511 051	-	-	-	-
Restated closing net book amount	-	511 051	58 152	67 472	12 272	648 947
Year ended 30 June 2005						
Restated opening net book amount	-	511 051	58 152	67 472	12 272	648 947
Additions	-	-	17 086	82 538	26 876	126 500
Reclassified	-	-	12 272	-	(12 272)	-
Amortization charge	-	-	(46 754)	(49 100)	-	(95 854)
Result of foreign exchange rate changes	-	14 803	-	-	-	14 803
Closing net book amount	-	525 854	40 756	100 910	26 876	694 396
At 30 June 2003						
Cost	-	-	59 767	62 597	10 764	133 128
Accumulated amortization	-	-	(8 443)	(42 616)	-	(51 059)
Net book amount	-	-	51 324	19 981	10 764	82 069
At 30 June 2004						
Restated cost	-	511 051	104 786	136 014	12 272	764 123
Accumulated amortization	-	-	(46 634)	(68 542)	-	(115 176)
Net book amount	-	511 051	58 152	67 472	12 272	648 947
At 30 June 2005						
Cost	-	525 854	134 144	218 552	26 876	905 426
Accumulated amortization	-	-	(93 388)	(117 642)	-	(211 030)
Net book amount	-	525 854	40 756	100 910	26 876	694 396

Amortisation of Ls 22 315 (2003/2004: Ls 16 889) is included in the "Cost of goods sold" in the income statement; Ls 58 237 (2003/2004: Ls 38 819) in "Selling and marketing costs"; and Ls 15 302 (2003/2004: Ls 8 409) in "Administrative expenses".

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Notes to the consolidated financial statements (continued)

10. Intangible assets (continued)

* The initial accounting for the business combination performed on 1 June 2004 was determined provisionally during the year ended 30 June 2004. During the reporting year the initial accounting for a business combination was completed. As a result the goodwill was allocated to 5 products' prototypes. Comparative information for the year before the initial accounting for the combination was completed is presented as if the initial accounting had been completed from the acquisition date.

The fair value of the product prototypes was determined based on the assessments of the value-in-use. Cash flow forecasts based on the next five-year budget approved by the Group's management were used in those calculations.

The following assumptions were used in fair value assessments of the product prototypes:

Financial year	2005	2006	2007	2008	2009
Gross margin % rate	0	49%	49%	49%	49%
Aggregate growth % rate	0	800%	319%	192%	170%
Discount % rate	0	11,40%	11,40%	11,40%	11,40%

The management determined expected gross margin based on the Group's past performance and its expectation for the market development. The growth rate calculation was subject to the assumptions on quantity of products sold and sales prices of specific products. Those assumptions were based on the management's forecasts for the market development and industry reports. The weighted average cost capital method was used in discount rate calculations.

An impairment test was performed on 30 June 2005 in order to determine the impairment loss of the prototypes. The result of the test showed no impairment loss; thus, no changes were made to the carrying value of the product prototypes.

11. Derivative financial instruments

	30.06.2005		30.06.2004	
	Assets Ls	Liabilities Ls	Assets Ls	Liabilities Ls
Forward foreign exchange contracts – cash flow hedges	-	8 988	4 446	468

12. Trade and other receivables

	30.06.2005 Ls	30.06.2004 Ls
Trade debtors	2 012 949	2 784 893
Provisions for bad and doubtful accounts receivable	(286 085)	(19 493)
Trade debtors, net	1 726 864	2 765 400
VAT receivable	13 345	147 422
Deferred expenses	61 491	20 748
Other debtors	6 512	42 095
Prepayment to suppliers	70 253	31 407
	1 878 465	3 007 072

Trade debtors includes undrawn Letters of Credit with original payment term of maximum 180 days for Ls 573 136 (2003/2004: Ls 1 832 225).

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Notes to the consolidated financial statements (continued)

12. Trade and other receivables (continued)

As at 30 June 2005 the fair value of trade and other receivables approximate their carrying values.

The increase of provisions for bad and doubtful accounts receivable is included into the income statement of the reporting year as Administrative expenses in amount of Ls 266 592 (2003/2004 – the decrease of Ls 20 257).

13. Inventories

	30.06.2005	30.06.2004
	Ls	Ls
Raw materials	1 944 988	1 084 916
Work in progress	2 198 079	1 613 406
Finished goods	431 421	312 330
Provisions for slow moving inventories	(208 706)	(73 676)
	<u>4 365 782</u>	<u>2 936 976</u>

The increase of provisions for slow moving inventories is included into the income statement of the reporting year as Cost of goods sold in amount of Ls 135 030 (2003/2004 – Ls 73 676).

14. Cash and cash equivalents

	30.06.2005	30.06.2004
	Ls	Ls
Cash in bank	50 184	60 977
Deposits in money market fund	-	553 632
Short – term bank deposits	55 006	237 648
	<u>105 190</u>	<u>852 257</u>

The effective interest rate on short – term bank deposits (overnight deposits) was 0,55% for Ls, 1,24% for USD and 0,6% for EUR.

15. Share capital

As at 30 June 2005 the subscribed, issued and fully paid share capital consists of 2 970 180 ordinary bearer shares with unlimited voting rights (2003/2004: 990 060 shares) with a nominal value of Ls 1 each.

The Company issued 1 980 120 new free bonus shares in December 2004 for existing shareholders.

16. Trade and other payables

	30.06.2005	30.06.2004
	Ls	Ls
Trade payables	362 468	484 944
Social security and other taxes	85 992	57 054
Accruals for unused annual leave	170 849	143 005
Payable for acquisition of business	-	131 949
Other creditors	128 029	102 292
	<u>747 338</u>	<u>919 244</u>

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17. Borrowings

	30.06.2005	30.06.2004
	Ls	Ls
Bank overdrafts	6 101	2 519

The fair values of the borrowings approximate their carrying values. All borrowings are due in less than 6 months after the balance sheet date. The balance of nused overdraft is Ls 24 304 as at 30 June 2005 (Ls 22 713 as at 30 June 2004).

18. Deferred income tax liabilities

	Year ended	Year ended
	30.06.2005	30.06.2004
	Ls	Ls
Deferred tax liability at the beginning of the reporting period	29 422	19 298
(Decrease)/ increase of deferred tax liability during the reporting period (Note 20)	(14 340)	10 124
Deferred tax liability at the end of the reporting period	15 082	29 422

Unrecognised deferred tax asset

	Year ended	Year ended
	30.06.2005	30.06.2004
	Ls	Ls
Unrecognised deferred tax asset at the beginning of the reporting period	19 599	-
(Decrease) / increase of unrecognised deferred tax asset during the reporting period (Note 20)	126 247	19 564
Currency translation differences	(619)	(5)
Unrecognised deferred tax asset at the end of the reporting period	145 187	19 559

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18. Deferred income tax liabilities (continued)

Deferred tax has been calculated from the following temporary differences between assets and liabilities values for financial and tax purposes:

	30.06.2005	30.06.2004
	Ls	Ls
Temporary difference on fixed assets depreciation and intangible asset amortisation (to be reversed during 12 months)	38 205	36 515
Temporary difference on fixed assets depreciation and intangible asset amortisation (to be reversed after more than 12 months)	29 545	14 769
Temporary difference on accruals for unused annual leave (to be reversed during 12 months)	(13 142)	(10 810)
Temporary differences on provisions for slow moving inventories (to be reversed during 12 months)	(24 802)	(11 052)
Temporary differences on tax losses carried forward	(159 911)	(19 559)
Unrecognised deferred tax asset	145 187	19 559
Deferred tax liability, net	15 082	29 422

No offsetting of deferred tax liabilities and assets arising at different jurisdictions has been performed.

Deferred income tax assets are recognised for SAF Sweden AB to the extent that the realisation of the related tax benefit through the future taxable profits is probable. The Group did not recognise deferred income tax assets of Ls 145 187 (2003/2004 – Ls 19 559).

19. Finance costs – net

	Year ended	Year ended
	30.06.2005	30.06.2004
	Ls	Ls
Interest expenses	27 562	113 783
Interest income	(2 934)	(11 329)
Net losses on foreign currency exchange rate fluctuations	12 512	149 568
	37 140	252 022

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20. Income tax expense

	Year ended 30.06.2005	Year ended 30.06.2004
	Ls	Ls
Increase / (decrease) in deferred tax liability (see Note 18)	(14 340)	10 124
Corporate income tax charge for the current period	399 622	877 599
	385 282	887 723

Corporate income tax differs from the theoretically calculated tax amount that would arise applying the 15% rate stipulated by the law to the Group's profit before taxation (2003/2004 – 19%):

	Year ended 30.06.2005	Year ended 30.06.2004
	Ls	Ls
Profit before taxation	1 967 976	4 808 292
Theoretically calculated tax at a tax rate of 15% (2003/2004 – 19%)	295 196	913 575
Tax effect from expenses not deductible for tax purposes	186 788	11 844
Effect of different tax rates	67 408	9 081
Tax relief for donations	(37 863)	(46 920)
Increase in unrecognised deferred tax asset	(126 247)	(19 564)
Effect of changes in enacted tax rates on deferred tax	-	19 707
Tax charge	385 282	887 723

Deferred tax is calculated by using the following enacted tax rates:

Year	Tax rate SAF Tehnika A/S	Tax rate SAF Tehnika Sweden AB
2003./2004.	19%	28%
2004./2005. and thereafter	15%	28%

In the period from 6 April 2004 till 2 July 2004 the State Revenue Service performed complex tax audit: audit of value added tax and corporate income tax with the auditing period of 2001 and 2002. In accordance with the State Revenue Service Decision on the audit results, corporate income tax for the year 2002 in amount of Ls 576 and corporate income tax penalty amounting to Ls 576 to be paid by the Company were additionally calculated. The Company has appealed to Administrative region court demanding to revoke this decision passed by the State Revenue Service. The Administrative region court discharged the Company's claim on cancellation of the State revenue Service decision.

The tax authorities may inspect the books and records for the last 2.5 years (starting from 1 January 2003) and may impose additional tax assessments with penalty interest and penalties. The Group's management is not aware of any circumstances, which may give rise to a potential material liability in this respect (The tax authorities have not performed all-inclusive tax inspection to date).

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Notes to the consolidated financial statements (continued)

21. Earnings per share

Basic earnings per share are calculated by dividing the profit with the weighted average number of shares during the year.

	Year ended 30.06.2005	Year ended 30.06.2004
Reporting period revenue (a)	1 559 327	3 920 569
Ordinary shares outstanding until 1 July*	2 970 180	2 970 180
Ordinary shares outstanding until 30 June*	2 970 180	2 970 180
Weighted average number of shares during the reporting period (b)*	2 970 180	2 970 180
Basic earnings per share at the reporting period (a/b), Ls	0.52	1.32

* The Group issued 1 980 120 dematerialized bearer bonus shares without making corresponding changes in the Group's resources on 1 December 2004. Because the bonus issue was without consideration, it is treated as if it had occurred before 1 July 2003.

The Group does not have dilutive potential ordinary shares.

22. Dividends per share

The dividends paid in the financial year 2004/2005 amounted to Ls 990 060 or Ls 1 per share (in 2003/2004: Ls 150 000 or Ls 0.75 per share). A dividend in respect of the financial year 2004/2005 of Ls 0.1 per share, amounting to a total dividend of Ls 297 018, is to be proposed at the Annual General Meeting on 26 October 2005. These consolidated financial statements do not reflect this dividend payable.

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23. Cash generated from operations

	Note	Year ended 30.06.2005 Ls	Year ended 30.06.2004 Ls
Profit before taxes		1 944 609	4 808 292
<u>Adjustments for:</u>			
- depreciation	9	457 586	269 255
- amortization	10	95 854	64 117
- changes in provisions for slow moving inventories		135 030	73 676
- changes in accruals for unused annual leave		27 844	108 007
- interest income	19	(2 934)	(11 329)
- interest expenses	19	27 562	113 783
- loss from revaluation of derivative financial instruments		12 966	-
Cash generated from operations before changes in working capital		2 698 517	5 425 801
Inventories increase		(1 563 836)	(986 242)
Receivables increase / (decrease)		898 386	(2 211 805)
Payables decrease		(199 977)	(154 472)
Cash generated from operations		1 833 090	2 073 282

24. Subsidiaries and business combinations

During the year ended 30 June 2005 no acquisitions of business or subsidiaries were made.

On 13 May 2004 the Group established a subsidiary SAF Tehnika Sweden AB by contributing cash of Ls 7 170 to the share capital. No goodwill arised on this transaction. SAF Tehnika Sweden AB is a 100% owned subsidiary of the Group, incorporated and domiciled in Sweden.

On 1 June 2004, subsidiary of the Group SAF Tehnika Sweden AB acquired Viking Microvawe business. The acquired business contributed revenues of Ls 70 141 and loss of Ls 69 872 for the period from 1 June to 30 June 2004. In a year ended 30 June 2004 business acquisition was accounted using provisional values. The initial accounting for the business combination was completed as described in Note 10.

Details of net assets acquired after the completion of initial accounting for the business combination are as follows:

	Fair value Ls
Purchase consideration (fully paid in cash)	768 474
Fair value of net assets acquired	(768 474)
Goodwill	-

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24. Subsidiaries and business combinations (continued)

The assets and liabilities arising from the acquisition are as follows:

	Fair value	Acquiree's carrying amount
	Ls	Ls
Intangible assets (product prototypes)	511 051	-
Property, plant and equipment	228 588	228 588
Inventories	109 636	109 636
Accruals for unused annual leave	(80 801)	(80 801)
Net assets	768 474	257 423

25. Related party transactions

Board and Council members' remuneration

	Year ended 30.06.2005	Year ended 30.06.2004
	Ls	Ls
Board members' remuneration		
· salary expenses*	97 172	70 015
· social insurance contributions*	17 801	14 012
Council members' remuneration		
· salary expenses*	65 198	72 083
· social insurance contributions*	15 123	16 348
Total	195 294	172 458

* Bonuses on year results are include in salary expenses and social insurance contributions.

One of the management members received short-term interest-free loan in the amount of Ls 7 000 at 15 December 2004. Loan was fully repaid at 31 January 2005.

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26. Personnel expenses

	Year ended 30.06.2005 Ls	Year ended 30.06.2004 Ls
Salary expenses*	1 270 422	612 746
Social insurance contributions*	345 416	148 214
Contributions to pension funds**	50 972	2 082
Total	1 666 810	763 042

* Salary expenses and social insurance contributions include provisions for the year performance results bonuses.

** Contributions to pension funds are made on behalf of personnel of SAF Tehnika Sweden AB.

27. Average number of employees of the Group

	Year ended 30.06.2005	Year ended 30.06.2004
Average number of personnel employed by the Group during the reporting period:	<u>124</u>	<u>104</u>

Average number of employees includes 14 employees, which were hired for subsidiary SAF Tehnika Sweden AB on 1 June 2004.

28. Operating lease

Lease agreement Nr. S-116/02, dated 10 December 2002, was concluded with Dambis A/S. In accordance with the agreement lessor commissions and SAF Tehnika A/S accepts premises with total area of 3 948 m² for the reimbursement. The premises are located at Ganibu dambis 24a. The agreement terminates on 1 March 2010.

In accordance with concluded agreements, the Group has the following lease payment commitments at 30 June 2005:

1 year	68 255
2 – 5 years	<u>216 140</u>
	<u>284 395</u>

29. Post balance sheet events

There are no subsequent events since the last date of the reporting year, which would have a significant effect on the financial position of the Group as at 30 June 2005.