

FINANCIAL STATEMENTS

of 1998

KLEMENTI LTD

TATEMENT BY THE CHAIRMAN OF THE BOARD

The year 1998 will be remembered as the year of economic slowdown in Estonia. The stock market crisis was followed by outflow of funds and supplemented by crises in Russia. Many companies lost their markets, many employees lost their income. Similar economic processes prevailed at our southern neighbours – Latvia and Lithuania.

In such complicated economic environment AS Klementi achieved the greatest growth of sales – 26.5% if compared to the previous year whereas the sales of women's fashion increased by 52.7%. But the plans had been bigger. In summer 1998 we recognised the first signs that our main markets – Latvia and Lithuania – are not capable of receiving our goods and marketing these.

To resolve the situation AS Klementi applied rather aggressive marketing policies by establishing two new stores and implementing other efficient marketing measures. As a result the most critical issue was solved – the sales of autumn-winter season goods. But the price was rather high to be paid – the five million net profit of the third quarter was reduced, after selective revaluation of inventories and making provisions for accounts receivable, to 1.6 million per entire year.

Considering the problems related to the Baltic market and Russia AS Klementi started a considerably more active marketing activity in western markets in 1998 by replacing its agents in Finland and Sweden and starting to market in Austria and England. Certainly these markets are more attractive because of their purchasing power but entering these markets is costly. However we are optimistic because the trade mark KLEMENTI is being established with good reputation in all the markets.

The year 1998 proved that rapid growth does not necessarily mean splendid financial results. Still, we consider it as success that we have adapted to the changed economic environment and founded the basis for our activity in 1999. Undoubtedly positive contribution has been made by the strategic investor of AS Klementi – the P.T.A Group OY who is the holder of 43% of shares since January 1999.

On behalf of the management board, I hereby confirm that AS Klementi will use all its powers to retain the value of shareholders' assets and provide conditions for adding value to these.

Madis Võõras
AS Klementi, Chairman of the Board

MANAGEMENT REPORT OF 1998

1. Products

In 1998 the business operations of AS Klementi and its subsidiaries were once again based on three different relatively independent business processes aimed at different markets:

- development, production and sales of women's fashion clothing (trade marks KLEMENTI and REGINA);
- development, production and sales of professional clothing (trade mark PROFLINE);
- subcontracting.

The two first are the company's original production, i.e. the manufacturing of which is financed by AS Klementi (trade marks Klementi and Regina) and AS Klementi's subsidiary AS Proflin (trade mark Proflin). Materials for work under subcontract are usually supplied and delivered by the customer.

The collection of classic women's clothing called BASIC BY KLEMENTI has been on the market since the end of 1997. The items of this collection can be purchased from the storage without advance order.

Net sales of AS Klementi and its subsidiaries were 124,579 th.kroons in 1998, which is 26,115 th.kroons or 26.5% more than in 1997. Division by business processes and other activities:

- women's fashion clothing 74,623 th.kroons (59,9 % of net sales), increase 52.7%
- professional clothing 18,091 th.kroons (14,5 %), increase 26.1%
- subcontracting (incl. sales of services) 29,307 th.kroons (23.5%), decrease 12.8%
- other (sales of materials, canteen etc.) 2,558 th.kroons (2.1%), increase 54.3%.

The sales volume of the company's original production was 92,714 th.kroons in 1998 (74.4 % of total turnover), out of which women's fashion clothing 80.5% and professional clothing 19.5%.

The summary of sales by markets is provided in the Notes to the financial statements.

In 1998 expenses on the development of new models were 3,496 th.kroons, i.e. 1,043 th.kroons (29.8%) more than in 1997.

2. Production

In 1998 the production activities of AS Klementi were mainly performed in the production facility with 395 workplaces for sewing workers located in Tallinn at Mustamäe.

During the period from January to September AS Klementi used the production volume of OÜ Deodora that was sold at the end of 1998 (45 workplaces).

The production volume in standard minutes (SM) was 26,322 th.SM in total, of which 1,956 th.SM was additionally purchased from other sewing companies as was necessary. In the Tallinn production unit of AS Klementi 24,367 th.SM were produced in 1998, which is 61,6 th.SM per working place (58,1 th.SM per working place in 1997, increase 6.2%).

3. Purchase policy

AS Klementi and its subsidiaries purchase raw materials mainly from the companies of European origin. This enables the duty-free import of ready-made products into the countries of the European Union, Latvia and Lithuania. Materials are purchased from about 60 companies. Total expenses on raw materials, goods and materials was 63,889 th.kroons (51.3% of net sales), increase was 23,019 th.kroons (56.3%) compared to 1997.

4. Personnel and salary policy

In 1998 AS Klementi and its subsidiaries employed 692 employees in average (61 persons, i.e. 8.1% less than in 1997), of them 505 employees directly in production (39 persons less than in 1997).

Labour expenses in 1998 were 48,222 th.kroons including social tax and medical insurance tax, increase 6,567 th.kroons (15.8%) compared to 1997. Labour expenses made up 38.7% of net sales.

The tariffs of task work increased 10% since 1 January 1998.

Since 1 January 1998 the salary of time workers was raised 10% in average.

The total time of absence of employees from work was 7.0% of the calendar normative work time, whereas the respective indicator was 8.7% among task workers of sewing shops (10.4% in 1997).

5. Investments

In 1998 the following investments were made:

- into the share capital of subsidiaries	3,012 th.kroons
- into tangible fixed assets	2,131 th.kroons
- into intangible assets	578 th.kroons
- into improvements of real estate	463 th.kroons
<hr/>	
TOTAL:	6,184 th.kroons

In 1998 the subsidiary Proflin owned 100% by AS Klementi was established, into the share capital of which AS Klementi's tangible and intangible assets used for manufacturing professional clothing were paid in as non-monetary payment.

Tangible fixed assets (mainly production machinery) were purchased for 2,131 th.kroons.

Investments into tangible fixed assets and intangible assets include the payments of lease and rent agreements concluded both before 1 January 1998 as well as during 1998.

The following items were acquired based on the new leasing agreement concluded in 1998:

- computer technology for the cutting department
- software for the cutting department
- self-service line "Metos" for the canteen
- car Mitsubishi Lancer.

6. Development of real estate

In 1998 the renovation and lease program of AS Klementi office building located in Tallinn at Akadeemia street 33 was continued. In 1998 reconstruction work and improvements of the real estate was completed for 463 th.kroons. The total volume of rent income in 1998 was 1,017 th.kroons.

7. Subsidiaries

The following subsidiaries belong to AS Klementi:

- OÜ Klementi Kinnisvara with share capital of 500 th.kroons, owned 100% by AS Klementi (management of AS Klementi's real estate);
- AS Proflin with share capital of 2,500 th.kroons, owned 100% by AS Klementi (production of professional clothing);
- Klementi Trading OY (registered in Finland) with share capital 131,6 th.kroons, owned 100% by AS Klementi (realisation of AS Klementi's production in Finland);
- AS Brendman with share capital of 100 th.kroons, owned 100% by AS Klementi (retail sales of women's clothes, no business operations in 1998).

8. Management board, meetings of the management board and salaries

As at 1 January 1998 the management board of AS Klementi consisted of the following members:

- Madis Võõras - Chairman of the Board
- Mare-Ann Perkmann - Vice-Chairman of the Board
- Urmas Rohi
- Lilia Peets.

Since 22 September 1998 Urmas Rohi is no longer a member of the board.

After the last change the management board of AS Klementi consists of three members who are the following:

- Madis Võõras – Chairman of the Board (General Manager)
- Mare-Ann Perkmann (Product Development Manager)
- Lilia Peets (Sales and Marketing Manager).

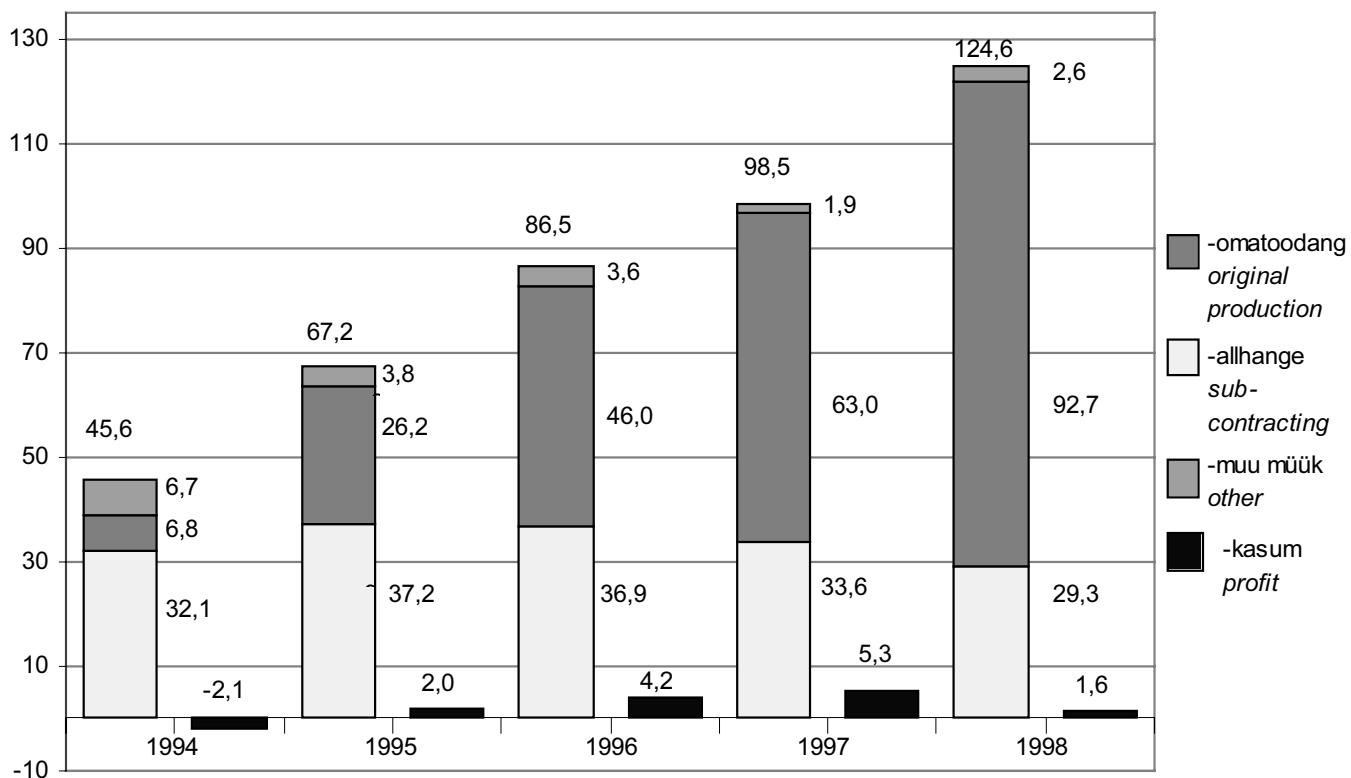
In 1998 28 meetings of the management board were held.

The members of the management board of AS Klementi are also the managers of the company. In 1998 salaries and bonuses in the total amount of 1,103 kroons were paid to the mentioned persons. Separate fee for participating in the work of the management board was not paid to the members of the board.

In 1998 the following persons belonged to the supervisory board: Ardo Kamratov (he is also the Administrative Manager of AS Klementi), Tambet Mägi and Elmu Puidet.

In 1998 13 meetings of the supervisory board were held. In 1998 the members of the supervisory board received 279,9 th.kroons in total for their work at the supervisory board, out of that 89,1 th.kroons for work in 1997 and 54,8 th.kroons for 1996.

AS Klementi kontserni käive ja kasum 1994a. - 1998a.
AS Klementi concern net sales and net profit in 1994 - 1998



Financial statements of 1998

*Balance sheet
As at 31 December 1998*

ASSETS

in kroons

	Parent company at end of fin. year 31 - Dec - 98	Consolidated at beg. of fin. year 31 - Dec - 97	Parent company at end of fin. year 31 - Dec - 98	Consolidated at beg. of fin. year 31 - Dec - 97	Change	%	Note
	1	2	3	4	1 - 2		
CURRENT ASSETS							
1. CASH AND BANK	2 174 088	2 929 446	1 457 479	2 844 909	-755 358	-25,79	1
2. MARKETABLE SECURITIES	369	294	369	294	75	25,51	2
3. CUSTOMER RECEIVABLES	17 462 445	9 723 294	14 334 327	9 693 979	7 739 151	79,59	3
4. OTHER RECEIVABLES	475 290	735 800	1 420 664	732 250	-260 510	-35,41	4
5. ACCRUED INCOME	828	1 985	828	1 548	-1 157	-58,29	5
6. PREPAID EXPENSES	405 384	987 620	231 956	935 821	-582 236	58,95	5
7. INVENTORIES	29 444 146	23 533 440	26 032 658	23 486 065	5 910 706	25,12	6
TOTAL CURRENT ASSETS:	49 962 550	37 911 879	43 478 281	37 694 866	12 050 671	31,79	
NONCURRENT ASSETS							
8. LONG-TERM FINANCIAL ASSETS	203 441	322 459	5 059 288	1 192 146	-119 018	-36,91	7;8
9. TANGIBLE FIXED ASSETS	30 804 298	33 115 709	30 615 030	32 556 806	-2 311 411	-6,98	9;11
10. INTANGIBLE ASSETS	2 162 801	2 339 307	1 858 451	2 332 628	-176 506	-7,55	10
TOTAL NONCURRENT ASSETS:	33 170 540	35 777 475	37 532 769	36 081 580	-2 606 935	-7,29	
TOTAL ASSETS :	83 133 090	73 689 354	81 011 050	73 776 446	9 443 736	12,82	

LIABILITIES AND OWNERS' EQUITY

in kroons

	<i>Consolidated</i> <i>at end of fin. year</i> 31 - Dec - 98	<i>Consolidated</i> <i>at beg. of fin. year</i> 31 - Dec - 97	<i>Parent company</i> <i>at end of fin. year</i> 31 - Dec - 98	<i>Parent company</i> <i>at beg. of fin. year</i> 31 - Dec - 97	<i>Change</i>	<i>%</i>	<i>Note</i>
	1	2	3	4	1 - 2		
LIABILITIES							
CURRENT LIABILITIES							
11. DEBT OBLIGATIONS	17 572 377	10 215 357	16 772 378	10 215 357	7 357 020	72,02	11;12;13
12. CUSTOMER PREPAYMENTS FOR GOODS AND SERVICES	94 377	54 807	78 601	54 807	39 570	72,20	
13. SUPPLIER PAYABLES	4 993 003	3 226 648	4 501 748	2 895 432	1 766 355	54,74	
14. OTHER PAYABLES	-	-	538 771	882 738	0	0,00	14
15. TAX LIABILITIES	3 463 891	1 472 551	2 494 101	1 310 185	1 991 340	135,23	14;16
16. ACCRUED EXPENSES	3 670 233	3 370 809	3 325 945	3 109 429	299 424	8,88	14
17. OTHER PREPAID REVENUE		217 918	-	217 918	-217 918	-100,00	14
TOTAL CURRENT LIABILITIES	29 793 881	18 558 090	27 711 544	18 685 866	11 235 791	60,54	
LONG-TERM LIABILITIES							
18. LONG-TERM LIABILITIES	15 816 473	19 216 026	15 816 473	19 216 026	-3 399 553	-17,69	11;12;13
19. DEFERRED TAX LIABILITY	41 771	-	-	-	41 771	100,00	16
TOTAL LONG-TERM LIABILITIES	15 858 244	19 216 026	15 816 473	19 216 026	-3 357 782	-17,47	
TOTAL LIABILITIES:	45 652 125	37 774 116	43 528 017	37 901 892	7 878 009	20,86	

in kroons

Parent company Consolidated Parent company Consolidated

	at end of fin. year 31 - Dec - 98	at beg.of fin. year 31 - Dec - 97	at end of fin. year 31 - Dec - 98	at beg. of fin. year 31 - Dec - 97	Change	%	Note
	1	2	3	4	1 - 2		
<i>OWNERS' EQUITY</i>							
19. SHARE CAPITAL PAR VALUE	24 250 000	24 250 000	24 250 000	24 250 000	0	0,00	15
20. SHARE PREMIUM	3 774 225	3 774 225	3 774 225	3 774 225	0	0,00	15
21. REVALUATION RESERVE	816 252	816 252	816 252	816 252	0	0,00	15
22. OTHER RESERVES	782 388	517 679	782 388	517 679	264 709	51,13	15
23. RETAINED EARNINGS	6 248 868	1 262 899	6 251 689	1 268 956	4 985 969	394,80	
24.NET PROFIT (LOSS) FOR THE FINANCIAL YEAR	1 609 232	5 294 183	1 608 479	5 247 442	-3 684 951	-69,60	
TOTAL OWNERS' EQUITY:	37 480 965	35 915 238	37 483 033	35 874 554	1 565 727	4,36	
TOTAL LIABILITIES AND OWNERS' EQUITY:	83 133 090	73 689 354	81 011 050	73 776 446	9 443 736	12,82	

INCOME STATEMENT

in kroons

Consolidated	Consolidated	Parent company	Parent company
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	Reporting year 01 - Jan - 98 31 - Dec - 98	Previous year 01 - Jan - 97 31 - Dec - 97	Reporting year 01 - Jan - 98 31 - Dec - 98	Previous year 01 - Jan - 97 31 - Dec - 97	Change	%	Note
	1	2	3	4	1 - 2		
REVENUE							
1. Net sales	124 578 696	98 463 647	117 513 696	98 305 239	26 115 049	26,52	17
2. Other revenue	702 729	905 487	1 324 754	916 046	- 202 758	-22,39	23
3. Change in work-in-progress and finished goods inventories	14 073 831	6 325 120	12 196 619	6 325 120	7 748 711	122,51	
EXPENSES							
4. Materials, consumables and supplies	63 889 318	40 870 597	59 157 252	39 957 850	23 018 721	56,32	24
5. Other operating expenses	16 526 839	10 207 775	17 316 112	12 009 171	6 319 064	61,90	25
6. Personnel expenses	48 221 809	41 654 771	46 137 248	40 369 272	6 567 038	15,77	26
incl. 6.a. wages and salaries	36 256 654	31 288 881	34 689 350	30 322 344	4 967 773	15,88	
6.b. social taxes	11 965 155	10 365 890	11 447 898	10 046 928	1 599 265	15,43	
7. Depreciation	3 681 140	2 574 119	3 629 440	2 558 409	1 107 021	43,01	9;10
incl. Depreciation of tangible fixed assets and value adjustments	3 681 140	5 574 119	6 629 440	2 558 409	1 107 021	43,01	
8. Other expenses	1 569 047	928 510	1 536 049	924 164	640 537	68,99	27
TOTAL EXPENSES:	133 888 153	96 235 772	127 776 101	95 818 866	37 652 381	39,13	
OPERATING PROFIT (LOSS)	5 467 103	9 458 482	3 258 968	9 727 539	-3 991 379	-42,20	

in kroons

	Consolidated Reporting year	Consolidated Previous year	Parent company Reporting year	Parent company Previous year	Change	%	Note
	01 - Jan - 98 31 - Dec - 98	01 - Jan - 97 31 - Dec - 97	01 - Jan - 98 31 - Dec - 98	01 - Jan - 97 31 - Dec - 97			

	1	2	3	4	1 - 2	
9. FINANCIAL INCOME						
9.1 Income from subsidiaries	875 958	-	3 134 500	144 959	875 958	100,00
9.3. Other interest and similar income	23 252	35 576	21 125	32 783	-12 324	-34,64
total:	899 210	35 576	3 155 625	177 742	863 634	2427,57
10. FINANCIAL EXPENSES						
10.1 Financial expenses related to subsidiaries	17 000	-	717 755	457 964	17 000	100,00
10.2. Interest expense	3 961 652	3 455 766	3 872 623	3 455 766	505 886	14,64
10.3. Foreign exchange loss	83 517	167 779	83 517	167 779	-84 262	-50,22
10.4. Other financial expenses	53 500	622	53 500	622	52 878	8501,29
total:	4 115 669	3 624 167	4 727 395	4 082 131	491 502	13,56
PROFIT (-LOSS)	2 250 644	5 869 891	1 687 198	5 823 150	-3 619 247	-61,66
FROM NORMAL OPERATIONS						
PROFIT (LOSS) BEFORE TAXES	2 250 644	5 869 891	1 687 198	5 823 150	-3 619 247	-61,66
INCOME TAX	599 641	575 708	78 719	575 708	23 933	4,16
DEFERRED INCOME TAX	41 771	-	-	-	41 771	100,00
NET PROFIT (LOSS) FOR THE FINANCIAL YEAR	1 609 232	5 294 183	1 608 479	5 247 442	-3 684 951	-69,60
EARNINGS PER SHARE	0,664	2,221	0,663	2,202		18

Cash flow

	Kontsern	Kontsern	AS Klementi	AS Klementi
	1998	1997	1998	1997
in kroons				
Cashflow from operating activities				

Adjustments from net profit				
Net profit	1 609 232	5 294 183	1 608 479	5 247 442
Depreciation of tangible fixed assets	2 876 159	2 187 672	2 857 791	2 171 962
Revaluation of tangible fixed assets	600 000		600 000	
Depreciation of intangible assets	804 981	386 447	771 649	386 447
Profit from sales of fixed assets	-52 811	-181 381	-52 203	-1 067 205
Profit from sales of securities	-875 958		-875 958	
Loss from sales of tangible fixed assets	4 448	8 702	3 969	8 702
Loss from write-off of tangible fixed assets	618 290	1 609	76 759	1 609
Profit from long-term financial investments			-1 557 788	1 230 313
Interests paid	77 395	317 767	77 395	317 767
Decline in value of shares	50 000		50 000	
Total	5 711 736	8 014 999	3 560 093	8 297 037
Adjustments from change of working capital				
Change in working capital	-12 806 030	-4 436 707	-9 500 354	-4 196 476
Change in short-term liabilities	3 801 375	-2 024 308	2 391 263	-1 896 533
Total	-9 004 655	-6 461 015	-7 109 091	-6 093 009
Total cashflow from operating activities	-3 292 919	1 553 984	-3 548 998	2 204 028
Cashflow from investing activities				
Purchase of securities			-231 604	-2 150 000
Money received from long-term receivables	69 018	21 275	69 018	71 275
Purchase of tangible fixed assets	-1 354 491	-5 534 849	-1 331 614	-5 525 103
incl. finance lease	881 060	2 507 265	881 060	2 507 265
Purchase of intangible assets	-628 475	-1 428 663	-577 896	-1 421 102
Sales of tangible fixed assets	81 047	392 154	79 547	1 841 963
Sales of securities	1 459 613		1 459 613	
Reconstruction of tangible fixed assets	-462 964	-2 884 705	-462 964	-2 884 705
Sales of subsidiaries	-583 655			
Total Cashflow from investing activities	-538 847	-6 927 523	-114 840	-7 560 407
Cashflow from financing activities				
Loans repaid	-4 000 000	-7 500 000	-4 000 000	-7 500 000
Loans received	8 172 689	13 000 000	7 372 689	13 000 000
Paid finance lease payments	-1 096 281	-1 540 216	-1 096 281	-1 540 216
Paid obligations of privatization		-5 571 546		-5 571 546
Received from issue of shares		5 762 307		5 660 621
Total cashflow from financing activities	3 076 408	4 150 545	2 276 408	4 048 859
TOTAL CASHFLOW	-755 358	-1 222 994	-1 387 430	-1 307 520
Cash at the beginning of period	2 929 446	4 152 440	2 844 909	4 152 428
Cash at the end of period	2 174 088	2 929 446	1 457 479	2 844 908

Movements in equity

kroonides / in kroons

	31.12.95	Change	31.12.96	Change	31.12.97	Change	31.12.98
1. Share capital	18 750 000		18 750 000	5 500 000 ⁽⁴⁾	24 250 000		24 250 000

2. <i>Share premium</i>	791 536	-11 734	⁽¹⁾	779 802	2 994 423	⁽⁴⁾	3 774 225		3 774 225
3. <i>Revaluation reserve</i>		816 252	⁽²⁾	816 252			816 252		816 252
4. <i>Mandatory legal reserve</i>		301 744	⁽³⁾	301 744	215 935	⁽⁵⁾	517 679	264 709	⁽⁶⁾ 782 388
5. <i>Retained earnings</i>					1 262 899	⁽⁵⁾	1 262 899	4 985 969	⁽⁷⁾ 6 248 868
6. <i>Current year profit</i>				4 210 950			5 294 183		1 609 247
<i>Total equity</i>	19 541 536			24 858 748			35 915 238		37 480 980
Aktsiate arv	1 875 000	-		1 875 000	550 000		2 425 000	-	2 425 000

- (1) Repurchase of shares from shareholders over par (with premium)
(2) Revaluation of land
(3) Mandatory legal reserve acquired with merger of AS Klementi and AS Klementi Kaubandus
(4) Increase of share capital according to decision of General Meeting of Shareholders on 28.02.97
Incl. 3 000 000 kroons fund issue and 2 500 000 kroons from shareholders
from subscription with share premium of 16 kroons (share price 26 kroons).
(5) According to decision of General Meeting of Shareholders on 28.02.97 legal mandatory
reserve was increased by 215 953 kroons and retained earnings by 1 262 899 kroons.
(6) According to decision of General Meeting of Shareholders on 15.05.98 legal mandatory
reserve was increased by 264 709 kroons.
(7) According to the decision of General Meeting of Shareholders at 15.05.1998 the retained earnings had to
be increased by 5 029 474 kroons. The difference -43 505 kroons arised from adjustments due to
calculating OÜ Deodora out from the consolidated financial statements

The Table illustrates changes in equity during the period from 31.12.1995 to 31.12.1998 for the Group.
As AS Klementi was registered in the Business Register as at 23.12.1996 after the merger of AS Klementi
and AS Klementi Kaubandus, the Table indicates AS Klementi's equity as at 01.01.1996 as that of the
merging company.
Differences between the changes in the equity of the Group and the parent company arise from the retained
which was 6 251 689 kroons of the parent company AS Klementi as at 31.12.1998.
This difference arises from adjustments made in connection with the sales of the subsidiary OÜ Deodora.
Also the net profit of the financial year is different. In 1998 the net profit of the parent company was
1 608 494 kroons, in 1997 5 247 442 kroons.

See also Note 15

Basis of Preparing the Financial Statements

The consolidated financial statements of AS Klementi (Group) and the financial statements of parent company (AS Klementi) have been prepared in conformity with the Estonian Accounting Law, the requirements of International Accounting Standards and good accounting practice. Financial statements have been presented in Estonian kroons.

Accrual Accounting Principle and Cost Principle are used in accounting of the Group of AS Klementi. Conservatism Concept is used at recording the potential income and expenses.

At preparing the current financial statements the updated IAS 1 has been applied first time, which will become valid during the reporting periods since 1 July 1998.

General Background of the Company

AS Klementi is a company that manufactures clothing products. The company began its business operations in 1944. In 1994 the privatisation process of AS Klementi started which was completed by fulfilling all terms fixed in the privatisation agreement before the Estonian Privatisation Agency in 1997.

The company is registered in Tallinn and its main activities are carried out in Tallinn. The company's headquarters are located in Akadeemia street 33, Tallinn.

In May 1997 AS Klementi was listed on Tallinn Stock Exchange secondary list.

In 1998 AS Klementi manufactured women's fashion clothing (trade marks KLEMENTI and REGINA), professional clothing (trade mark PROFLINE) and subcontracted mainly with Finnish and Swedish customers.

Since 1 September 1998 AS Klementi's subsidiary AS Proflin manufactures the professional clothing. In 1998 major part (48.7%) of the production of AS Klementi was exported. The main export countries were Finland, Sweden, Latvia and Lithuania.

In 1998 AS Klementi invested 2,5 million kroons into the share capital of its subsidiary AS Proflin (100% ownership), 131,6 th.kroons into Klementi Trading OY operating in Finland and 100 th.kroons into AS Brendman that did not have business operations in 1998.

In 1998 the renovation and lease program of AS Klementi office building was continued; the volume of investments was 463 th.kroons.

Consolidation Principles

The present financial statements include the consolidated financial statements of AS Klementi and its subsidiaries OÜ Klementi Kinnisvara, AS Proflin, Klementi Trading OY and AS Brendman.

The consolidated financial statements have been prepared by adding up the separate lines from income statements and balance sheets of the above mentioned companies, whereas all sales-and-purchase transactions between the group companies, mutual receivables and liabilities are eliminated.

The companies where AS Klementi owns over 50% of the share capital are considered subsidiaries. At the acquisition of subsidiaries goodwill is calculated as the difference between the purchase price and the share acquired in the company's equity as at the acquisition date. Goodwill is depreciated over 5 years. Subsidiaries will be consolidated since the month following the acquisition date.

AS Klementi had no associated companies (share 20 - 50%) in 1997 and 1998.

Accounting policies

Inventories

Inventories are recorded at the lower of cost or net realisable value. Inventories of material are recorded at acquisition cost based on the weighed average method. Work-in-progress and finished products are recorded at projected cost.

Noncurrent physical assets

Assets with useful life over one year and cost 2,500 kroons or more are recorded as fixed assets. Tangible fixed assets (ex. land and buildings) are recorded at acquisition cost in the balance sheet. Land and buildings are recorded at the re-valued amount. Accumulated depreciation is recorded on a separate line in the balance sheet.

Depreciation is calculated according to the straight-line method, which is based on useful life. In 1997 and 1998 the following depreciation rates were used:

- production facilities	3%
- other buildings	10%
- machinery	10%
- computer equipment	20%
- transport vehicles	20%
- other fixtures and equipment	25 - 30%

Repair and maintenance costs are expensed as incurred or capitalised as tangible fixed asset if the useful life of the underlying asset is significantly prolonged.

Low-value assets are expensed 100% at acquisition.

Intangible assets

In 1996 the development costs of trade mark KLEMENTI were recorded as intangible assets. The development costs were increased in 1997. The costs of developing, appropriation and registration of the trade mark PROFLINE have been recorded in the balance sheet as at 31 December 1998. The trademark development costs will be depreciated over 5 years.

Software is also recorded in the balance sheet under intangible assets. In 1998 software was acquired for 578 th.kroons.

Depreciation on intangible assets is calculated according to the straight-line method, based on useful life of the assets (3 to 5 years).

Valuation of receivables

Customer receivables and other receivables are recorded in the financial statements on accrual basis. Reserve has been made for uncollectible receivables. During the period from 1 January 1998 to 1 November 1998 0.35% of net sales was transferred into the reserve. Since 1 November 1998 0.5% of net sales has been transferred into the reserve. Additionally the receivables have been re-valued as necessary once a quarter at the end of the quarter.

Long-term financial investments

As at 31 December 1998 AS Klementi had four subsidiaries, which are recorded in the balance sheet of the parent company AS Klementi on the line "Shares of subsidiaries" under long-term financial assets based on the equity method. Financial investments in the balance sheet of the parent company are re-valued based on the equity method once a quarter. The last valuation was carried out as at 31 December 1998.

In the Group's financial statements the subsidiaries are consolidated according to separate entries.

Loan interest

Interest paid on loans is expensed as incurred.

Deferred Tax

26% income tax is paid on taxable profit according to calculations at the end of the year. Advance payments are recorded as prepayments until the income tax return is filed in.

Deferred tax liability (or asset) is accrued in balance sheet from all timing differences between the assets and liabilities of tax and accounting calculation. The timing differences between tax and accounting calculations arise from the differences of principles in Income tax legislation and in accounting. The major timing differences arise from depreciating tangible fixed assets and carry-forwards of tax losses.

In 1998 the new IAS 12 was applied that came became effective 01.01.1998. The applying of the new IAS 12 did not bring about significant changes in the deferred tax amount.

Vacation Pay Accrual

Once a year there is annual vacation for production workers of AS Klementi. For correct periodisation of expenses AS Klementi calculates vacation pay reserve constantly. The reserve is accrued monthly as 13.5% of calculated salaries.

Accounting for Leasing

Capital leases and operating leases are recorded according to Instruction No.10 on Lease Accounting issued by the Estonian Accounting Board on 15 August 1997 that became effective on 1 January 1998. The lease transaction is recorded as operating lease in all cases where both of the following circumstances exist:

- the lessor could terminate the lease relation unilaterally without making additional payments before the fulfilment of terms set in the lease agreement or the termination of the lease period.
- ownership of the leased asset object does not transfer to the lessor during or its termination.

If the above mentioned conditions have not been fulfilled, the lease is recorded as capital lease.

The tangible fixed assets acquired under the terms of capital lease are recorded at the present value of the lease payments. The rent payments have been recorded under short- and long-term borrowings, interest expense is expensed when it arises. The assets acquired under capital lease contract are depreciated according to the useful life of the asset, analogically with other tangible fixed assets.

The rent payments of tangible fixed assets under operating lease are recorded as rent expense when they arise. The assets are not accrued in balance sheet and are not depreciated.

Assets that have been leased out by a group company on terms of operating lease are recorded as tangible fixed assets and are depreciated according to their useful life. Rent income is recorded when it arises.

This treatment is in accordance with IAS.

Sales

Sales are recorded using the Accrual Principle based on the transfer of rights from seller to purchaser.

Cash Flow Statement

Cash Flow Statement of AS Klementi is prepared using the indirect method, according to which net profit is adjusted by eliminating the effect of nonmonetary transactions, investing operations, financing operations and changes in current assets and current liabilities in order to calculate the operating cash flow. In Cash Flow Statement cash and cash equivalents includes cash in the company and deposits on demand on the company's bank accounts.

Foreign Currencies

All assets and liabilities denominated in foreign currencies are recorded as restated with the average exchange rates of the Bank of Estonia as at 31 December 1997. Estonian Kroon is connected with the Deutsche Mark at the rate 1DEM=8EEK.

Segments

Sales by activities and markets are provided in the Notes to the financial statements. All of the production is located in Estonia. Division of assets and net profit between segments can not be determined and therefore such division has not been provided.

Notes to financial statements

In the tables included in the Notes to financial statements the financial indicators are provided in thousands kroons. The division of assets and liabilities by period is provided in Table 8.

Note 1. Cash and bank

	<i>Group</i>		<i>AS Klementi</i>	
	1998	1997	1998	1997
Cash	242	110	175	93
Bank accounts	1,249	2,366	668	2,298
Foreigncurrency accounts	683	453	614	453
	2,174	2,929	1,457	2,844

Note 2. Marketable securities

On the balance sheet line "Marketable securities" the service record booklets and additional pages thereto have been recorded as monetary documents. Shares of other companies have not been recorded in the balance sheet under short-term financial assets.

Note 3. Accounts receivable

	<i>Group</i>		<i>AS Klementi</i>	
	1998	1997	1998	1997
Customer receivables	17,962	9,723	14,834	9,694
Reserve for uncollectible receivables	- 500	-	- 500	-
	17,462	9,723	14,334	9,694

No provisions for uncollectible receivables were made in the financial statements of 1997. The respective provisions were made since 1 January 1998. As the market situation worsened, an additional provision for receivables was made in September 1998 in the amount of 2,000 th.kroons. During 1998 and 1997 receivables were expensed in the total amount of 1,668 th.kroons and 262 th.kroons respectively. The reserve for uncollectible receivables in the amount of 500 th.kroons has remained in the balance sheet as at 31 December 1998, as all receivables for sales in 1998 may not be collected at the beginning of 1999.

Note 4. Customer receivables

	<i>Group</i>	<i>AS Klementi</i>
	1998	1998
OÜ Norrison (according to purchase-sale contract of shares)	160	160
Loans given to individuals	118	118
Prepayments to suppliers	103	94
Receivable from pension authority	29	29
Loans given to third parties	20	20
Receivable from AS Võru Rõivas	20	20
Other receivables	25	23
AS Proflin	-	740
Klementi Trading OY	-	216
Kokku	475	1,420

	<i>Group</i>	<i>AS Klementi</i>
	1997	1997
Receivable from AS Jõgeva Rõivas	200	200
OÜ Norrison (according to purchase-sale contract of shares)	80	80
Loans given to third parties	100	100
Export Council	100	100
Prepayments to suppliers	95	95
Receivable from sale of own shares in 1997	46	46
Loans to individuals	63	63

Other receivables	52	48
Total	736	732

The balances of consolidated financial statements agree in material part to the balances of the parent company. In the consolidated financial statements of 1998 the 9 th.kroons prepayment to suppliers of AS Proflin and 2 th.kroons receivable from reporting persons have been recorded in addition to the balances of the parent company.

Note 5. Other receivables

Interest receivable from banks in the amount of 0.8 th.kroons in 1998 and 2 th.kroons in 1997 are recorded as accrued income.

	Group		AS Klementi	
	1998	1997	1998	1997
Prepaid taxes	176	821	34	769
Other prepaid expenses	229	167	198	167
	405	988	232	936

Prepaid corporate income tax in the amount of 24 th.kroons and 152 th.kroons prepaid VAT are recorded under "Prepaid taxes" in 1998 consolidated financial statements of AS Klementi. Prepaid taxes of 1997 include 103 th.kroons of corporate income tax prepayment and 718 th.kroons of prepaid VAT.

Other prepaid expenses are insurance payments, rent prepayments, subscriptions of periodicals etc.

AS Klementi and its subsidiaries do not have any receivables from the members of supervisory board, management board and other related persons.

The division of payment of receivables by period is provided in Table 8.

Note 6. Inventories

	Group		AS Klementi	
	1998	1997	1998	1997
Raw materials	7,344	6,816	6,090	6,806
Work-in-progress	7,042	9,026	7,037	9,026
Finished goods	14,877	7,045	13,049	7,045
Merchandise purchased for resale	513	203	190	166
Prepayments to suppliers	130	443	129	443
Inventory write-down reserve	-462	-	-462	-
	29,444	23,533	26,033	23,486

In 1998 the total of finished goods and work-in-progress (current assets) written down was 5,377 th.kroons (in AS Klementi 5,355 th.kroons) and 401 th.kroons (in AS Klementi 379 th.kroons) was written off. In 1997 the total of current assets written down was 458 th.kroons and 182 th.kroons was written off.

Note 7. Long-term financial assets

	Group		AS Klementi	
	1998	1997	1998	1997
Shares of subsidiaries	0	0	4,856	870
Other shares	0	50	0	50
Other long-term receivables	203	272	203	272
	203	322	5,059	1,192

The main part of other long-term receivables in 1998 is the debt of OÜ Norrison in the amount of 100 th.kroons for purchasing shares by instalments and 60 th.kroons remainder of a loan acquired by quitclaim. In 1997 the debt of OÜ Norrison was 200 th.kroons.

The nominal value of the share capital of **OÜ Klementi Kinnisvara** (owned by AS Klementi 100%; operating in Estonia; managing the real state of the parent company AS Klementi in Tallinn) is 500 th.kroons – recorded at 300 th.kroons in the balance sheet of the parent company. The company started its business activities on 1 July 1997.

The nominal value of the share capital of **AS Proflin** (owned by AS Klementi 100%; operating in Estonia; manufacturing professional clothing) is 2,500 th.kroons, consisting of 250,000 shares with nominal value 10 kroons – recorded at 4,377 th.kroons in the balance sheet of the parent company. The company was established in 1998 and started its business activities on 1 September 1998.

At establishing the company AS Klementi's assets were paid into the subsidiary's share capital as non-monetary payment. The following assets were included in the share capital of AS Proflin:

- fixed assets in total amount of 710,491 kroons
- low-value items in total amount of 5,680 kroons
- original models in total amount of 113,784 kroons
- basic cut-out patterns of models in total amount of 24,256 kroons
- finished goods in total amount of 1,125,912 kroons
- basic material in total amount of 1,059,877 kroons.

The trade mark PROFLINE in the amount of 280,424 kroons was transferred to AS Proflin. The mentioned sum is recorded in share premium of the subsidiary. The liability from customer prepayments made to the parent company in the amount of 1,783,306 kroons was transferred to AS Proflin. As at establishing actually more assets were transferred into the subsidiary, the balance of mutual receivables and liabilities ended up in the receivable of the parent company in the amount of 1,344,312 kroons as at 1 September 1998.

The nominal value of the share capital of **Klementi Trading OY** (owned by AS Klementi 100%; registered and operating in Finland; realisation of AS Klementi's products in Finland) is 50 th. FIM – recorded at 81 th.kroons in the balance sheet of the parent company. The company was established in September 1998 and started its business activities on 1 October 1998. The company was established by monetary payment into the share capital. The revaluation of assets and liabilities has been made by using the exchange rate 1FIM=2,63207EEK as at 31 December 1998.

AS Brendman (owned by AS Klementi 100%; operating in Estonia; trading and intermediation). The company had no business operations in 1998. Its share capital 100,000 kroons was purchased for 117,000 kroons. In the 31 December 1998 balance sheet the company's net assets are recorded at 100,000 kroons. Goodwill has been expensed in AS Klementi at purchasing the shares of the subsidiary.

AS Klementi owns 12,5% of the shares of **AS Eesti Ettevõtjate Ärikeskus** with nominal value 50 th.kroons. As the company's business operations have been stopped and according to the audited balance sheet as at 31 December 1998 the company's net assets do not meet the requirements of the Commercial Code Article 301, the company has been recorded in AS Klementi's balance sheet at "0" value.

The subsidiary **OÜ Deodora** (was owned by AS Klementi 100%; operating in Estonia); that was sold was removed from the balance sheet as at 30 September 1998. The value of the sold financial asset as at 31 December 1997 was 583,655 kroons. 1,459,613 kroons, which was also the sales price, was received from the sales. Financial income from the sales transaction is recorded in the 1998 income statement in the amount of 875,958 kroons. At the moment of ownership transfer (30 September 1998) the assets of OÜ Deodora were 1,445,882 kroons which was divided as follows:

- current assets total 301,998 kroons, incl. cash in hand and in bank 2,367 kroons;
- inventories total 2,152 kroons;
- fixed assets total 1,143,884 kroons.

At that moment the equity of OÜ Deodora was 1,179,613 kroons and total liabilities 266,269 kroons. Majority of the liabilities consisted of tax payables (154,236 kroons) and accrued expenses (88,482 kroons).

The following will illustrate the business operations of AS Klementi's subsidiaries in 1998:

According to 31 December 1998 balance sheet (in kroons)

	OÜ Klementi Kinnisvara	AS Proflin	Klementi Trading OY
Total assets	702,986	7,346,197	326,357
Total current assets	675,814	6,877,683	326,357
incl. cash and bank	65,093	580,228	71,287
Total noncurrent assets	27,172	468,514	0
Total liabilities	403,018	2,971,039	245,637
incl. total current liabilities	403,018	2,929,268	245,637
owners equity	299,968	4,375,158	80,720
incl. share capital	500,000	2,500,000	131,604

According to 1998 income statement (in kroons)

	OÜ Klementi Kinnisvara	AS Proflin	Klementi Trading OY
Total revenue	5,186,004	11,417,072	167,338
incl. net sales	5,184,967	9,535,287	167,338
Total expenses	5,172,117	9,172,693	218,221
incl materials, consumables and supplies	2,215,637	5,861,337	63,920
incl. personal expenses	1,625,418	459,142	0
financial income	49	2,077	0
financial expenses	0	89,029	0
profit (loss) before taxes	13,936	2,157,427	-50,883
net profit (loss) for the financial year	13,936	1,594,734	-50,883

Mutual receivables and liabilities between the parent company and subsidiaries are the following:

- AS Proflin and the parent company
 - AS Proflin payable to AS Klementi for sewing services in the amount of 740,155 kroons as at 31 December 1998;
 - in 1998 AS Proflin has purchased sewing services and materials from AS Klementi for 3,977 th.kroons in total; in 1998 AS Klementi has purchased finished goods and materials from AS Proflin for 111 th.kroons in total.
- OÜ Klementi Kinnisvara and the parent company
 - AS Klementi payable to OÜ Klementi Kinnisvara for maintenance services of premises and industrial electricity in the amount of 1,148,536 kroons as at 31 December 1998. OÜ Klementi Kinnisvara payable to AS Klementi for accounting, administration and human resource services in the amount of 709,765 kroons as at 31 December 1998. AS Klementi's debt according to the balance sheet is 438,771 kroons in total;
 - in 1998 AS Klementi has purchased maintenance services of premises, industrial electricity and household materials from OÜ Klementi Kinnisvara for 4,791 th.kroons in total. In 1998 AS Klementi has sold accounting, administration, HR services and communication services and materials to OÜ Klementi Kinnisvara for 732 th.kroons in total.
- Klementi Trading OY and the parent company
 - in 1998 Klementi Trading OY has purchased finished goods from AS Klementi for 82,315 FIM, i.e. 216,659 kroons; Klementi Trading OY payable to AS Klementi as at 31 December 1998 is of the same amount;
 - in 1998 AS Klementi has purchased market research from Klementi Trading OY for 35,000 FIM, i.e. 92,089 kroons.

In transactions with related parties regular prices have been used.

Note 8. Long-term loans given

AS Klementi has given loans neither to shareholders, members of the supervisory and management board nor to other related parties. Prior to the privatisation of the company in 1994 long-term loans to farmers and local municipalities had been given. The balance of those loans was 0 kroons as at 31

December 1998 (in 1998 the 3,5 th.kroons loan to a farmer was written off). The maturity date of the loan is the year 2002.

The following has been recorded under long-term receivables as at 31 December 1998:

- long-term part (100 th.kroons) of the receivable from OÜ Norrison with the payment date 1 December 2000;
- long-term part (10 th.kroons) of the receivable from AS Võru Rõivas, which was taken over from AS Klementi Kaubandus during the merger;
- long-term part (33 th.kroons) of the loan given to an individual with maturity date of 1 March 2001;
- long-term part (60 th.kroons) of the loan given to a farmer by Eesti Maapank at the company's guarantee with payment date 1 October 2002 acquired by quitclaim.

Note 9. Tangible fixed assets

	Group		AS Klementi	
	1998	1997	1998	1997
Land and buildings	26,969	26,918	26,969	26,403
Plant and equipment	12,815	12,552	12,805	12,111
Other equipment and fixtures	4,809	4,068	4,332	4,042
Accumulated depreciation	-14,463	-12,499	-14,165	-12,076
Fixed assets under construction	674	2,076	674	2,076
Prepayments for fixed assets	-	1	-	1
	30,804	33,116	30,615	32,557

On 25 June 1996 revaluation of land and buildings was carried out, whereby the price of land was complied with its market value. The revaluation amount of land is recorded as part of the equity in the amount of 816 th.kroons under "Revaluation reserve". The price of land before revaluation was 982 th.kroons.

The buildings were re-valued in the balance sheet due to the merger of AS Klementi and AS Klementi Kaubandus (merger agreement signed as at 19 July 1996) by 12,2 million kroons, which was transferred to the equity as revaluation reserve of the merging entity in accordance with the merger agreement. The residual value (carrying amount) of buildings before revaluation was 6,829 th.kroons. After the revaluation the carrying amount of buildings was 19,000 th.kroons. If the buildings were not re-valued, the residual value as at 31 December 1998 would be 6,360 th.kroons not including the improvements made after the revaluation. In connection with the merger the revaluation of buildings was transferred into restricted equity.

Both revaluations were carried out by an independent expert AS Ober Haus.

In 1997 and 1998 no revaluations of tangible fixed assets were made.

In 1997 the administrative building was renovated. The renovation work was partly capitalised by adding its value to the carrying value of buildings in the amount of 2,885 th.kroons. In 1998 renovation work was capitalised in the amount of 463 th.kroons. Improvements are depreciated over 10 years.

In 1998 the tangible fixed assets of the sold subsidiary OÜ Deodora in acquisition cost 956 th.kroons are not recorded in the Group's balance sheet. At the establishment of subsidiaries no tangible fixed assets have been acquired outside the Group. The movement of tangible fixed assets related to the establishing of subsidiaries has occurred inside the Group. In 1997 there were no tangible asset movements outside the Group related to the establishment or sales of subsidiaries.

As at 31 December 1998 a building under construction was written down by 600 th.kroons into net realisation value 300 th.kroons from the profit of 1998.

As at 31 December 1998 fully depreciated fixed assets (of "0" value) were on account in AS Klementi at acquisition cost 5,312 th.kroons. On 31 December 1997 the respective amount was 4,614 th.kroons.

Tables illustrating the movement of fixed assets are enclosed to the financial statements (Tables 1 - 4).

Note 10. Intangible assets

	Group		AS Klementi	
	1998	1997	1998	1997

<i>Acquisition cost on 1 January</i>	2,877	1,448	2,869	1,448
<i>Acquired during the year</i>	628	1,429	578	1,421
<i>Transferred to the subsidiary's equity during the year</i>	-	-	318	-
<i>Acquisition cost on 31 December</i>	3,505	2,877	3,129	2,869
<i>Accumulated depreciation on 1 January</i>	538	151	536	151
<i>Depreciation calculated during the year</i>	804	387	735	385
<i>Residual value on 31 December</i>	2,163	2,339	1,858	2,332

Accrued development costs of trade marks in acquisition cost as at 31 December:

"KLEMENTI"	498	498	498	498
"PROFLINE"	318	318	0	318

The increase of the rest of intangible assets in 1997 was related to the improvement of production preparation and management by the purchased software. In 1998 intangible assets increased only due to software purchases.

At establishing the subsidiary AS Proflin the trade mark PROFLINE was transferred to the subsidiary including accumulated depreciation. By that amount the intangible assets of AS Klementi as the parent company were decreased. By the end of 1998 the carrying amount of trade marks KLEMENTI and PROFLINE were 318 th.kroons and 252 th.kroons respectively.

Note 11. Capital and Operating Lease

As at 31 December 1997 the balance of unpaid redemption sums of fixed assets acquired by capital lease was 2,117 th.kroons in total in the balance sheet. In 1997 asset redemption sums in the total amount of 1,540 th.kroons, contractual fees of 35 th.kroons and interest of 239 th.kroons were paid. As at 31 December 1998 the balance of unpaid redemption sums of fixed assets acquired by capital lease was 1,902 th.kroons in total in the balance sheet. In 1998 asset redemption sums in the total amount of 1,096 th.kroons, contractual fees of 6 th.kroons and interest of 260 th.kroons were paid. In 1999 1,085 th.kroons is due and the long-term part of capital lease is 816 th.kroons. No additional obligations to AS Klementi result from the valid lease agreements.

In 1997 AS Klementi had one operating lease agreement in force, related to Lectra cutting complex. Total operating lease payments in 1997 were 590 th.kroons.

The operating lease of Lectra cutting complex has been accounted for as capital lease since the end of 1997. In 1998 AS Klementi leased equipment from other parties, for the usage of which the total of 533 th.kroons was paid.

All lease agreements are concluded by the parent company.

The amounts of future payments related to lease agreements with the maturity date up to 1 year is 1,900 th.kroons and from 1 to 5 years 816 th.kroons.

Tables on capital lease agreements are attached (Tables 5 - 6).

Note 12. Short- and long-term loans

AS Klementi has the following loan obligations as at 31 December 1998:

	short-term	long-term	interest
Secured loans:			
- Estonian Union Bank overdraft	4,500	-	14.5%
- Estonian Union Bank loan for current assets	7,000	-	17%
- Loan of Estonian Investment Bank	3,000	15,000	DEM Libor+6.75%
- Advance payment of Estonian Union Bank factoring	373	-	18,5%
Unsecured loans:			
- leasings	1,085	817	11,4%
- liability to Innovation Fund	814	-	0%
	16,772	15,817	

AS Klementi had the following loan obligations as at 31 December 1997:

	short-term	long-term	interest
Secured loans:			
- Tallinna Pank overdraft	5,500	-	11.2%
- Loan of Estonian Investment Bank	3,000	18,000	DEM Libor+6.75%
Unsecured loans:			
- leasings	901	1,216	10.06%
- liability to Innovation Fund	814	-	0%
	10,215	19,216	

In the tables above the debt obligations of AS Klementi as the parent company have been provided. The overdraft of AS Proflin from Estonian Union Bank in the amount of 800 th.kroons and annual interest 15% should be added to the Group debt obligations. AS Klementi is planning to decrease the working capital loan by 2,000 th.kroons in February 1999 and 2,000 kroons in March 1999.

In 1997 the liability to the Innovation Fund increased by 377 th.kroons, as AS Klementi acquired the respective liability of the sold subsidiary AS Jõgeva Rõivas. After that there was receivable from AS Jõgeva Rõivas in the same sum, which has been paid off by the end of 1998. The maturity date of the liability to the State Innovation Fund (State Budget) has not been fixed. The mentioned liability bears no interest.

The loan of the Estonian Investment Bank is due 15 November 2004. The final due date of lease agreements is the year 2000.

Note 13. Loan Collateral and Assets Pledged

Collateral for the long-term loan taken from the Estonian Investment Bank are first the contracts of setting mortgage on to the real estates of administrative building, production building, auxiliary production building and the building of shop of 29,500 th.kroons and second the contract of commercial pledge of 15,000 th.kroons.

The collateral of the overdraft taken from Tallinna Pank is first the contract of commercial pledge of 23,000 th.kroons concluded in 1997 and second, the contract of setting mortgage on the above mentioned real estate of 10,000 th.kroons.

In 1998 AS Klementi as the parent company has given no additional collateral or pledged assets. AS Proflin has pledged 2,000,000 kroons to Estonian Union Bank as collateral for a loan taken.

Note 14. Other Short-term Payables

The liability to OÜ Klementi Kinnisvara of 439 th.kroons and a loan from AS Brendman 100 th.kroons are recorded under other payables in the balance sheet of the parent company.

Tax liabilities are recorded in the balance sheet as follows:

	Group		AS Klementi	
	1998	1997	1998	1997
- personal income tax	1,454	652	1,361	609
- income tax from fringe benefits	10	4	10	4
- social security tax	855	550	809	511
- health insurance tax	253	197	224	177
- VAT	311	60	30	-
- income tax	521	-	-	-
- total tax fines payable	60	9	60	9
	3,464	1,472	2,494	1,310

Accrued expenses in the company's balance sheet are the following:

	Group		AS Klementi	
	1998	1997	1998	1997
Salary-related accrued expenses	2,952	2,812	2,751	2,551

- salaries to employees	1,668	1,546	1,567	1,421
- vacation reserve	1,255	1,239	1,155	1,104
- other payables to employees	29	27	29	26
Interest payable	395	317	395	317
- interest payable to Estonian Investment Bank	239	270	239	270
- interest payable to Union Bank	156	47	156	47
Other accrued expenses	323	241	180	241
- Rent payments by AS Multiehitus	180	180	180	180
- other accrued expenses	143	61	-	61
	3,670	3,370	3,326	3,109

The prepaid rent payments are recorded under other prepaid revenue as at 31 December 1997. The total amount belongs to the parent company.

Note 15. Owners' equity

The **share capital** of AS Klementi is 24,250 th. kroons which is divided into 2,425,000 A-shares with the nominal value of 10 kroons. A-shares provide one vote at the general meeting of shareholders. No bill of share is issued. The share register is electronic and is kept in the Estonian Central Depository for Securities. According to the company articles the maximum capital of AS Klementi can be 75,000 th. kroons.

AS Klementi had 946 shareholders as at 31 December 1998.

Klementi shareholders as at 31 December 1998

Name	Number of shares	Share in share capital
<i>Share of major shareholders</i>	1,117,040	46,06%
OÜ Fine Holding	790,890	32,61%
OÜ Softleks	168,680	6,96%
The Baltic Growth Fund	157,470	6,49%
<i>Shares of members of the Council</i>	0	0
<i>Shares of Members of the Board</i>	5,500	0,22%
incl. Peets, Lilia	5,000	0,21%
Perkmann, Mare-Ann	500	0,00%
<i>Shares belonging to small shareholders</i>	1,302,460	53,72%
TOTAL SHARE CAPITAL	2,425,000	100,00%

Formation of share capital

80% of the shares of AS Klementi were privatised on 30 March 1994. The share capital of AS Klementi right after privatisation (statutes registered in Tallinn City Council on 8 June 1994) was 18,750 th. kroons. In 1994, 1995 and 1996 the share capital of AS Klementi was not increased. The decision on the increase of share capital was adopted at the General Meeting of Shareholders of Klementi on 28 February 1997. The share capital was decided to increase by 5.5 million kroons by issuing 550,000 new A-shares with the nominal value of 10 kroons for that purpose.

The issue was acquired as follows:

Shares

- bonus issue	300,000 shares
- closed subscription (EEK 26 per share)	190,000 shares
- subscription right the managing directors, members of the Management Board and Council (EEK 13.3 per share)	60,000 shares

In addition, according to the decision of the regular general meeting as at 28 February 1997 the contract of share option was concluded for motivating the managing directors of AS Klementi, on 20,300 shares with the price 13.3 kroons per share. For fulfilling the terms of the contract of option AS Klementi purchased the shares from the secondary market with the average price of 22.91 kroons

The shares of AS Klementi were acquired with the above-mentioned option by the Members of the Council Tambet Mägi and Ardo Kamratov and the Members of the Management Board Madis Võõras, Mare-Ann Perkmann, Lilia Peets and Urmas Rohi. The shares were acquired with the contract of option by 21 persons in total.

In 1997 and in 1998 no dividends were paid to shareholders. In 1996 the dividends of 9.3% of the nominal value of shares were paid to shareholders. In 1997 the shareholders acquired by bonus issue new shares in the amount of 16% of the total nominal value of shares. In 1998 no changes were made in share capital.

Share premium

	31.12.1998	31.12.1997
Share premium at 1 January	3,774	780
Share issue	-	3,329
Loss from option contract	-	335
Loss from share repurchase	-	-
Share premium at 31 December	3,774	3,774

All movements in the group share premium balance are related to movements in the share premium of parent company.

In 1998 no changes were made in share premium.

Reserves

	31.12.1998	31.12.1997
Revaluation reserve	816	816
Revaluation reserve arose from revaluation of land at the end of 1996.a.		
Mandatory legal reserve at 1 January	518	302
Legal reserve prepared from profit	264	216
Mandatory legal reserve at 31 December	782	518

Mandatory legal reserve was formed according to Commercial Code, Art. 336, p.3 - 5% of profit.

All changes in the group reserves are related to changes in the reserves of the parent company.

Retained earnings

	31.12.1998	31.12.1997
Retained earnings at 1 January	6,557	4,211
Bonus issue	0	-3,000
Formation of mandatory legal reserve	-264	-216
Correction to former periods	- 44	266
Retained earnings at 31 December	6,249	1,263
Profit for the financial year	1,609	5,294

Retained earnings balances in 1996 show zero as in cause of the merger of AS Klementi and AS Klementi Kaubandus in 1996 restricted equity was adjusted by non-restricted equity. Adjustment of

retained earnings by 44 th. Kroons in 1998 was caused by exclusion of OÜ Deodora's assets and liabilities from the group balance sheet.

Dividends are prepared for in balance sheet only after the general meeting has made relevant decision.

Note 16. Taxes calculated and paid

In 1997 the profit before taxes of AS Klementi (parent company) was 5,823 th. kroons. As the company was operating with loss during the previous years, there were carryforwards of income tax loss. A deferred income tax asset of 1,300 th. kroons was not recorded, because management had no clear evidence that timing differences from carryforwards of tax losses would reverse. In 1997 the deferred income tax asset was used for decreasing the taxable income and thus 576 th. kroons of income tax was to be paid.

In 1996 AS Klementi paid income tax in the amount of 492 th. kroons from the dividends paid to the shareholders, by which the income tax liability was reduced in 1997. According to the 1998 income tax return, the income tax payable by AS Klementi (parent) was 79 th. kroons and income tax payable by the group was 600 th. Kroons.

In 1998 tax authorities determined the corporate income tax prepayments to be paid by AS Klementi for 1999 at 48 th. kroons per month (total 576 th. Kroons).

Income tax calculated and to be paid

	<i>Group</i>		<i>AS Klementi</i>	
	1998	1997	1998	1997
Calculated profit in the Estonian accounting	3,859*	5,510*	1,687	5,823
<u>Taxable profit is increased by</u>				
Increase of profit according to Estonian tax laws	1,375	1,572	1,345	1,572
Depreciation in financial statements	3,681	2,589	3,629	2,558
Other	82	2,912	82	2,630
Total increase in profit	5,138	7,073	5,056	6,760
<u>Taxable profit is decreased by</u>				
Increase of loss according to Estonian tax laws	3,285	3,921	3,264	3,921
Tax depreciation	3,388	523	3,176	523
Total decrease in profit	6,673	4,444	6,440	4,444
Use of tax losses from the previous years	17	5,925	-	5,925
Taxable profit	2,307	2,214	303	2,214
Income tax to be paid	600	576	79	576

* The total of tax return entries "Profit before taxes" (unconsolidated).

Deferred tax (DT)

When AS Klementi and AS Klementi Kaubandus were united, deferred tax asset recorded off balance sheet was recorded to AS Klementi. Deferred tax asset appeared from losses carried forward from

1993-1996. Due to that deferred tax asset AS Klementi had no income tax liability in 1996. In 1997, after using rest of deferred tax asset from loss carry forward AS Klementi accrued income tax liability of 576 th. kroons. In 1998 the income tax liability of AS Klementi (parent) was 79 th. kroons and the income tax liability of the group totalled at 600 th. kroons. Temporary differences in accounting and tax calculation which caused the balance of the deferred income tax asset/liability on 31 December were as set below.

Deferred tax has been calculated according to the established income tax rate 26%.

	<i>Group</i>		<i>AS Klementi</i>	
	1998	1997	1998	1997
Deferred tax asset at the beginning of the year	77	1,300	0	1,300
DT liability from difference in depreciation in tax and accounting calculation	-171	321	-130	241
DT asset from tax losses carried forward	-27	-1,544	0	-1,541
DT asset from provisions for doubtful accounts	130	0	130	0
Total deferred income tax expense	-68	-1,223	0	-1,330
Deferred tax asset at the year end of the year	9	77	0	0

	<i>Group</i>		<i>AS Klementi</i>	
	1998	1997	1998	1997
Total DT asset	207	1,621	130	1,541
Total DT liability	-198	-1,554	-130	-1,541
DT liability at year end	9	77	0	0

DT assets and liability has been balanced as they relate to the same business entity.

Deferred tax asset is not recorded in the balance sheet.

Balance sheet follows the DT assets to the extent it is covered by liability.

Note 17. Net sales

The consolidated net sales of AS Klementi in 1998 was 124,579 th. kroons (including the export of 60,732 th. kroons or 48.7%) and 98,464 th. kroons in 1997 (including export 57,276 th. kroons or 58.2%) which comprised of the following:

1998	Group		Parent company	
	sales	incl. export.	sales	incl. export
- self-production and goods	92,714	32,876	83,480	32,787
- contractual works	27,376	26,936	27,376	26,936
- sale of materials	1,098	450	2,153	449
- sale in canteen	1,460	-	1,464	-
- sale of services	1,931	470	3,041	470
Total	124,579	60,732	117,514	60,642

1997	Group		Parent company	
	sales	incl. export.	sales	incl. export
- self-production and goods	63,212	24,766	63,174	24,766
- contractual works	32,190	31,783	32,190	31,783
- sale of materials	384	108	369	108

- sale in canteen	1,273	-	1,273	-
- sale of services	1,404	620	1,299	620
Total	98,464	57,276	98,305	57,276

The main destinations of export were:

Countries	1998	1997
Finland	29,595	36,793
Sweden	5,698	9,990
Lithuania	13,066	4,795
Latvia	9,537	4,218
Germany	-	1,014
CIS	1,416	-
Other	1,420	466
Total	60,732	57,276

See also Table 7

The company's assets and net profit are not distributed between segments as relevant information is not clearly distinguishable. In the opinion of the company's management the distribution could be based on the sales proportion. All operations of company and all the assets are placed in Estonian.

Note 18. Earnings per share

Earnings per share is calculated in accordance with International Accounting Standard (IAS 33).

	Group		AS Klementi	
	1998	1997	1998	1997
Number of shares at 1 January	2,425,000	1,875,000	2,425,000	1,875,000
Shares issued	0	550,000	0	550,000
Number of shares on 31 December	2,425,000	2,425,000	2,425,000	2,425,000
Profit	1,609	5,294	1,608	5,247
Number of shares	2,425,000	2,383,333**	2,425,000	2,383,333**
Earnings per share in kroons	0,664	2,221	0,663	2,202

** As the bonus issue in 1997 brought about no additional financial resources for the company, the number of shares for 1997 has been changed.

1997 $((1,875,000 + 300,000) * 12/12) + (250,000 * 10/12) = 2,383,333$

AS Klementi had no potential ordinary shares in both periods (1997 and 1998) and therefore the diluted earnings per share is the same as the basic earnings per share.

Note 19. Contingent liabilities

AS Klementi has no contingent liabilities as at the date of compiling the financial statements.

Note 20. Off-balance sheet liabilities

As at 31 December 1998 AS Klementi has guaranteed the loans of its employees with the letters of guarantee to Eesti Hoiupank of 60 th. kroons and AS Profline's (subsidiary of Eesti Ühispank) overdraft of 800 th.kroons. The given guarantees are recorded off-balance sheet.

Note 21. Insured assets

AS Klementi has insured the following assets:

Assets	Insured value	
	1998	1997
Buildings	110,000	37,800
Equipment and cars	27,000	3,079
Office and computer equipment	4,536	716
Raw materials and finished goods	27,900	9,500

In addition to property insurance the company has obtained business interruption, fire damage, water damage and technical risk insurance policies in the amount of 83,000 th.kroons (with liability period of 12 months and idle period of 72 hours).

Note 22. Additional notes to income statement

The reason of increase in balances of finished goods by 2,488 th. kroons in 1997 was the fact that already in November 1997 (i.e. significantly earlier than previous years) the production of spring collection of 1998 and the new "Basic" collection under the trademark "Klementi" was started.

The increase of finished goods balance by 7,832 th.kroons in 1998 was mainly caused by smaller sales volume of own products than estimated in autumn 1998, also because of losing the Russian market. It was planned to sell 2/3 of the mentioned products during the first half of 1999.

The increase in balances of work-in-progress by 3,837 th. kroons in 1997 compared to 1996 was also due to the earlier beginning of producing the spring collection. In addition the increase of ratio (ratio of indirect production costs per standard minute) regarding the production costs by 0.57 points had an effect on the growth of work-in-progress. The share of materials in the cost of work-in-progress in 1997 makes total of 6,594 th. kroons or 73.06%. There was a decrease of the balance of work-in-progress in 1998 (decrease of 1,984 th.kroons). The share of materials in the cost of work-in-progress in 1998 was 4,270 th.kroons, i.e. 60.6%.

Note 23. Other revenue

	Group		AS Klementi	
	1998	1997	1998	1997
Income from rent of rooms	69	315	69	315
Income from sale of fixed assets	52	181	52	150
Income from other realisation	377	148	1,000	190
Compensations	205	1261	204	261
Total	703	905	1,325	916

Rental payments for premises received by AS Klementi in January 1998 were recorded under other revenue. Starting from February 1998 rental payments were documented as revenue from the normal operations of OÜ Klementi Kinnisvara.

Note 24. Materials, consumables and supplies

	Group		AS Klementi	
	1998	1997	1998	1997
Raw materials	56,919	34,959	52,356	34,833
incl. write-down	5,377	458	5,335	442
write-off	401	182	379	174
Goods	4,399	2,998	4,354	2,907
incl. goods of canteen	1059	890	1059	890
Electricity and fuel	2,571	2,914	2,447	2,218
Total	63,889	40,871	59,157	39,958

Note 25. Other operating expenses

	1998	Group		AS Klementi	
		1997	1998	1997	
Production and company operating expenses	12,650	7,688	13,820	8,898	
incl. Bad receivables	2,293	262	2,168	292	
Sewing service purchased	2,766	1,828	2,415	2,419	
Business trips	740	692	725	692	
Taxes	371	-	356	-	
Total	16,527	10,208	17,316	12,009	

Note 26. Personnel expenses

	1998	Group		AS Klementi	
		1997	1998	1997	
Salaries of employees	23,182	20,653	22,128	19,791	
Salaries of administration	13,075	10,636	12,561	10,531	
Social taxes	11,965	10,366	11,448	10,047	
Total	48,222	41,655	46,137	40,369	

Note 27. Other expenses

	1998	Group		AS Klementi	
		1997	1998	1997	
Write-down of assets under construction	600	-	600	-	
Foreign exchange loss	129	201	120	201	
Membership fees	279	228	272	225	
Contract fees	-	130	-	130	
Change in rate of EPV	-	95	-	95	
Sponsoring	146	81	146	81	
Tax interests	86	68	84	67	
Deficiencies in stock count	101	43	101	43	
Loss from disposal of fixed assets	77	-	77	-	
Fine for quality	44	28	44	28	
Compensation for damage	41	-	41	-	
VAT	37	28	37	27	
Fines	1	8	0	8	
Other	28	19	14	19	
Total	1,569	929	1,536	924	

Note 28. Main subsequent events

On 28 January 1998 a Finnish textile company P.T.A. Group OY acquired 1,041,138 shares of AS Klementi, i.e. 42.9% of the company's share capital.

Note 29. Risks related to company's business activities and the opinion of the management on risk management**Credit risk**

Credit risk indicates the potential loss incurred from the inability of business partners to fulfil their obligations taken. Foremost the ability of major clients to pay for the goods supplied in time is of importance. The company enables the credit to its major business partners (for ex. AS Agdeck, AS Snoby, AS Maraave, Latvian company Neo Prim). Credit is given due 30 to 60 days with limits of up to 300 to 1,000 th. kroons.

The company made provision for the doubtful receivables starting from 1998. The reserves not used in 1998 in the amount of 500 th.kroons have been carried forward to 1999.

Foreign currency risk

48.7% of the sales of AS Klementi of 1998 was export. The main part of materials for production is purchased outside the Republic of Estonia. The major currencies the company deals with every day are EEK, DEM, FIM, SEK, FRF and ITL. The expenses are mainly in EEK, FIM, SEK, FRF, DEM and ITL and the income is distributed between EEK, FIM, SEK and DEM. The company is open to fluctuations of FIM and SEK in relation to EEK. For hedging the foreign currency risk company has not used any forwards, options or other financial instruments, as the management of the company has analysed and reached conclusion that potential losses from open foreign currency positions do not exceed the cost of using financial instruments to hedge those risks.

Liquidity risk

AS Klementi is constantly planning the cash flow. The plan is reviewed twice a month. The level of free cash for immediate use is kept at 1,500 - 2,000 th. kroons constantly to secure need for purchase of materials, fulfilling obligations in front of employees and other current obligations.

Interest risk

The company's interest risk depends on fluctuations of DEM Libor (see also Note 12).

The management representation on the accuracy and completeness of the preparation of 1998 financial statements of AS Klementi parent company and the group is presented on pages of the annual report.