INet Inc.

DUNS Number: 552479917

Annual Report 2007

Enter a World of Excellence in Technology

June 2008

Headquarters

Company Name:	INet Inc.
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DUNS Number :	552 479 917
CEO:	Toni Petreski toni@inet.com.mk

Corporate Facts

Legal Structure:	Joint Stock (2000)
Ownership:	100% Private
Year of Foundation:	1991
# of Employees:	15
# of Distributions:	9
# of Customers:	40+ Business Partners contracts
2007 Turnover EUR:	2.473.691
2007 Net Profit EUR:	53.312
Stage:	Red Hat regional market leader

Distribution Agreements

IBM Business Partner; lenovo Business Partner	*Authorized Distributor & Authorized Warranty Service Provider (for Macedonia and Kosovo)*
CHANNEL SAP PARTNER	*Sales & Services Partner (for Macedonia, Albania and Kosovo)*
redhat ADVANCED PARTNER	*Advanced Partner (for Macedonia, Albania and Kosovo)*
redhat. CERTIFIED TRAINING PARTNER	*Red Hat – Certified Training Partner (for Macedonia, Albania and Kosovo)*
TREND MICRO PREMIUM PARTNER	*Premium Partner (for Macedonia, Albania and Kosovo)*
xerox	*Authorized Distributor*

ENTER A WORLD OF EXCELLENCE IN TECHNOLOGY AND DISCOVER THE MACEDONIAN MOST FAVOURABLE IT DISTRIBUTOR

The door is open. Beyond the threshold, people are connecting, networking, e-commercing. The lines between our homes and offices are blurring. The boundaries between the nations and cultures are thinning. It's a world of difference out there and INet is making a difference - at the forefront of the excellent technology - by offering an array of solutions and services to numerous resellers and by regionally distributing and marketing IT products from many suppliers.

INet Today

INet has been in the business of Information and Communication Technology (ICT) on the Macedonian market since 1991. The company is highly recognized in value-oriented technology distribution and channel innovation providing complex ICT equipment, peripherals and packaged software products while adding value through technical capabilities.

Having adopted a modern organizational structure, INet has established three self-directed work business teams (departments) acting as profit centers: **INet Sales**, **INet Business Services, INet Center of Excellence**. Through these departments, while seeking new opportunities, INet is growing and developing its activities that correspond to different market segments and serve different needs.

Products and Services Highlights

Stepping inside reveals wide product offering – from network and systems solutions to peripherals and software. Add to that INet's entrance into the open source community and the company has created a strategic, diversified mix of products and services that in 2007 generated EUR 2.5 million in sales.

Our strategy could never succeed if the relationship between INet and our supplier-partners did not embrace and support it. Partnership agreements with our best partners: IBM, Lenovo, SAP, Red Hat, Trend Micro, Xerox… guarantee the quality, wide portfolio and professionalism of our company.

Competitive Differentiation

Being distinctively better than rivals on one or more Key Success Factors (KSFs) presents a golden opportunity for gaining competitive advantage. INet's distinctive competitively important internal activities (core competencies) reside in cross-department combination of skills and resources: strategic partnership with suppliers, efficient ICT products distribution capability, skills in choosing quality ICT products, attractive mix of built-in performance features, much-better-than average reliability, and very good after-sales and technical support services.

A key factor to our success today and in a future is a strategy that helps INet to run the business more effectively. Production, marketing, human, capital and other resources must always be capable of fulfilling the company's strategy. We choose the following strategic best practices because we wanted to let our customers know that we are committed being a world-class IT company:

- **Quality Enablers**. Project & Portfolio Management– adoption of the TenStep (www.tenstep.com) Project & Portfolio Management methodology;
- **Quality Methodologies**:
  - IT Mark certification – adopted in February 2007;
  - Development and introduction of new IT services based on the ITIL v.3 best practices framework.
  - Total Quality Management Culture - superior customer service standards, 24-hours spare parts availability, 100% "accuracy and guaranteed response times" to fully satisfy customer expectations for prompt service, a full range of technical support activities, team-based work design, involvement and empowerment of employees at all levels by appropriate motivation and rewarding system;
- **Information Technology**. Value Chain Information System implementation - a rollout of SAP Business Suite, a family of open, integrated solutions that manage the entire value chain. We install SAP web based support information system for improved customer, sales and service operations, employee, supplier / partner / collaborative ally, financial performance and to provide the management with the key operating data.
- **Governance Strategy**. Corporate Governance implemented in 2007, based on IFC (World Bank) methodology, to strengthen the shareholders value.

Indeed, **the door is open**. Beyond the threshold is a company at the forefront of a growing, vibrant industry – a company that has created a **winning formula** of strong management, a careful yet innovative diversification strategy and an

Customer Base

INet serves its business partners and their business likely serves a diverse mix of customers who rely on them to solve their IT challenges.

- *IT Channels Companies* - Corporate Resellers (Resellers), Small Office/Home office (SOHO)/Consumer Retailers & Dealers
- *IT Hardware Companies* & PC Assemblers (System Builders)
- *IT Software Companies* - Independent Software Vendors (ISVs), Local ERP Specialists, Local Accounting Application Providers, Local Horizontal & Vertical Application Providers, Other Small Local ISVs
- *IT Services Companies* - System Integrators (Solution Providers), Value Added Resellers (VARs), IT Training and Education Specialists
- *Telecom Carrier Services Companies* - Telecom Carriers, Fixed Telephony Operators, Mobile Network Operators, Internet Service Providers (ISPs), Cable Operators, Wireless Operators;
- *Other Telecom Companies* - Telecom Distributors, Telecom Support Companies, Telecom Equipment Companies

Market Perspective

According to IDC (2007), the **IT services** opportunities are much bigger than the other IT sectors, because of:

- The steadily growing proportion of IT services in overall ICT demand.
- Offering the IT services containing more value-added (managed services, outsourcing).
- Small groups of high-skilled and innovative professionals could achieve respectful results.
- Barriers to entry the developed countries IT markets are likely to be weaker compared to the other ICT sectors.

Information Technology Infrastructure Library (ITIL) is becoming the next big thing in IT. It is the new industry buzz-word, the new certification, the new conference, and the new idea that the IT world feels it needs. ITIL describes a framework of processes for the management of IT. Since INet works in the IT industry, and plans to work for a medium-to-large organizations in a future, INet has to add one or more ITIL certifications in its resume.

The ITIL implementation journey is long-term one since it is measured in years not in months. ITIL is a new approach to continuous improvement which has its own goal to provide IT services in a more cost-effective manner and to better match those services to the present and the future needs of our business partners unwavering **commitment to our business partners**.

New Services Opportunities

Still more doors are opening before us — opportunities for expansion that include the rocketing demand for wireless mobility, including notebook computers, smart handhelds and POS products; the convergence of consumer and commercial markets; the automation of the home; and thousands of small and medium sized businesses in need of complete IT solutions. And yet, in the world of IT distribution, success is anything but "in one door and out another". Which is why, at INet, our IT solutions go beyond distribution to offer a broad selection of programs and services. Among them – logistics, marketing and financial solutions for our retailing partners; training, marketing and technical assistance for our reseller customers. As a result of this complete approach to our business, 2007 saw us once again outperform our peers and generate profit levels not seen since 2000.

New Markets Opportunities

Even more doors continue to open for us – particularly in Albania and Kosovo where INet is the only distributor for Red Hat products, services and solutions.

Management Team

The management team consists of:

- Toni Petreski, BSc.Eng., Executive MBA, President and CEO (toni@inet.com.mk);
- Nadezda Dimitrovska, BSc.Eng., COO and Center of Excellence Manager (nade@inet.com.mk);
- Slobodan Stojcevski, BSc.Eng., Sales Department Manager (bobis@inet.com.mk);
- Aspasija Tasevska, BSc.Ecc., Finance & Controlling Manager (aspa@inet.com.mk);

Board of Directors

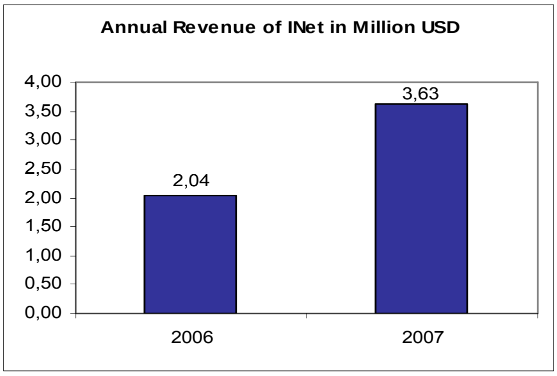
The Board of Directors of INet consists of 5 members: Mr. Toni Petreski, Ms. Nadezda Dimitrovska, Ms. Aspasija Tasevska and Mr. Slobodan Stojcevski, inside members of the Board, and Mr. Aleksandar Naumovski BSc.Eng. (alex@inet.com.mk), an outside member of the Board of Directors.

Community Groups Membership

- MASIT - Macedonian Association of Information Technology (www.masit.org.mk). MASIT is a voluntary, non-profit association and organizational form of all private companies whose basic activities are manufacturing, trading and services in the area of information technology, and which are registered on the territory of Republic of Macedonia.
- United Nation's Global Compact Initiative (www.unglobalcompact.org). INet Inc. is among the first Macedonian companies that joined Global Compact initiative in January 2005, embracing and supporting the ten universal principles of corporate social responsibility as part of its operations.
- HRDF - Human Resources Development Fund (www.enterpriselearning.org.mk). INet is one of the founders of the HRDF. It is constituted as a program of the European Agency for Reconstruction at the Ministry of Economy of the Republic of Macedonia.

Financial Results

We distribute and market hundreds IT products which our clients require and our revenue mix by product category has grown over the past several years.



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BUSINESS

The following discussion includes forward looking statements, including but not limited to, management's expectations of competition; revenues, margin, expenses and other operating results or ratios; operating efficiencies; economic conditions; cost savings; liquidity; capital requirements; exchange rate fluctuations and rate of return.

Introduction

INet has been in the business of Information and Communication Technology (ICT) on the Macedonian market since 1991. It is highly recognized in the fields of sales, distribution, rental and services of ICT products, ICT based business solutions, education and consulting. This focused strategy has permitted INet to increase both revenues and profits over the years. The company has established three self-directed business teams: ICT Product Distribution, ICT Support Services and ICT Consulting, in order to grow and develop in these businesses while seeking new opportunities. Our strategy could never succeed if the relationship between INet and our supplier-partners did not embrace and support it. Exclusive agreements with our best partners: IBM, Lenovo, SAP, Red Hat, Trend Micro, Xerox… guarantee the quality, wide portfolio and professionalism of our company. In 2006, INet opened doors of opportunity by signing agreements with new vendors and by expanding the product portfolio. The year was a significant turning point, as the company charged ahead, and remained focused on improving operations, enhancing efficiency and customer focus.
Today our company is stronger, more agile and better prepared for the future than ever before.

Industry

IT products and services distribution industry generally consists of two types of business: traditional distribution business and fee-based supply chain services business.
Within the traditional distribution model, the distributor buys and sells products and/or services to resellers who, in turn, typically sell directly to end-users, or other resellers. Hardware manufacturers and other publishers, which we collectively call suppliers or vendors, sell directly to distributors, resellers and end-users. As demand for supply chain services grows, distributors will seek new opportunities to provide services within and outside of the IT sector to complement their traditional distribution business. Fee-based supply chain services include the supply chain components that ensure the flow of goods from origin to consumption.
The traditional IT distribution industry continues to change as a result of a number of factors. As margins have narrowed on hardware products due to commoditization trends as technology evolves along its life cycle, suppliers and resellers have transitioned from a more product-focused to a more solution-oriented business model. Suppliers have also reduced the number of distribution partners and believe that suppliers continue to embrace two-tier distributors and are able to deliver products to market in a low cost manner. Resellers in the traditional distribution model continue to depend on distributors for a number of services, including product availability, marketing, credit, technical support, and inventory management. As resellers adjust their business models from selling products to selling solutions, they rely on distributors to help them combine products with services to complete the solutions they offer to their customers. As resellers require more solution-oriented offerings, distributors respond with enhanced value-added solutions and services customized to the needs of their specific customer base. A variety of reseller categories exist, including value-added resellers (""VARs"), corporate resellers, systems integrators, direct marketers, independent dealers, PC assemblers, and consumer electronics ("CE") retailers. Different types of resellers are defined and distinguished by the end-user market they serve, such as large corporate accounts, mid-market, small-to-medium sized businesses (""SMBs"), or home users, and by the level of value they add to the basic products they sell.
Many of our reseller customers are heavily dependent on distribution partners with the necessary systems, capital, inventory availability, and distribution facilities in place to provide fulfilment and other services.

Company Strengths

The following strengths enable us to further enhance our leadership position in the IT sector:

- *Leading Market Reach* - We believe that we are one of the leaders in the IT sector in this region offering large products and services in the IT industry. Our scale allows us to purchase products in large quantities and avail ourselves of purchase opportunities from a broad range of suppliers and provide competitive pricing for our reseller customers. Our reseller customers can derive purchasing efficiencies and reduce their investment in inventory while simultaneously enhancing end-user service levels by establishing a supply relationship with us. This relationship ensures resellers meet their product inventory needs through a single point of contact rather than purchasing product directly from multiple suppliers. We believe that we also provide suppliers with access to a broad customer base that few can reach directly in a more cost-effective manner.

- *Strong Working Capital and Financial Position* - We have consistently demonstrated strong working capital management in both positive and difficult economic conditions. In particular, we have maintained a strong focus on optimizing our investment in inventory, while minimizing the deployment of debt. We are reducing our inventory days as result of our focused and sustainable initiatives towards reducing excess and obsolete goods, better buying strategies, and a cultural orientation towards return on invested capital. Furthermore, we continue to manage our accounts receivable through collections, credit limit setting, customer terms and process efficiencies to minimize our working capital requirements.
- *Our business process improvement programs* have also resulted in improving profitability, providing us with a solid foundation for growth. Based on the strength of our balance sheet and improving profit trends, we also believe that we are well positioned to support our growth initiatives in our core business and/or invest in incremental profitable growth opportunities.
- *Superior Execution and Vital Link in the Supply Chain.* - We are committed to increasing our value to our customers and suppliers as a vital link in the IT distribution and technology supply chain. Through our understanding and fulfilment of the needs of our reseller and supplier partners, we provide our customers with the tools they need to increase the efficiency of their operations, enabling them to minimize inventory levels, improve customer delivery, and enhance profitability. Critical to our superior execution is our ability to provide quick and efficient order fulfilment along with consistent, accurate and on-time delivery to our customers. We provide business information to our customers, suppliers, and end-users by leveraging our information systems. We give resellers, and in some cases their customers, real-time access to our product inventory data.
- *Enlarging the product portfolio* – The Company established excellent collaboration relations with several worldwide vendors:
  - ***IBM*** - IBM Business Partner – Distributor
    IBM Authorized Service Provider
    IBM Authorized Training Provider
    IBM PartnerWorld Member

  In year 2005, INet has signed agreements with recognized vendors that are well identified at the regional market such as:
  - ***SAP*** – SAP Channel Partner
  - ***Lenovo*** - Lenovo Business Partner – Distributor
    Lenovo Authorized Service Provider
  - ***Red Hat*** - Red Hat Advanced Partner
    Red Hat Certified Training Partner
  - ***Trend Micro*** - Trend Micro Premium Partner

  In year 2007, INet has signed an agreement with Xerox:
  - ***Xerox*** - Xerox Authorized Distributor

The signed agreements for mutual collaboration provide the company to enlarge its product portfolio, and to define new strategies for growth in order to become recognized on the regional market.

Vision, Mission, Values

Vision

INet to be universally regarded as the best way to deliver technology in Macedonia and in the Balkan region.

Mission

To help our business partners grow and be more profitable, while maximizing value for our shareowners, by:

- Broadening the reach of our business partners, connecting them with new markets, technologies and solutions
- Earning the respect and loyalty of our business partners through superior value and service
- Creating innovative ideas through bright, energetic, customer-focused and talented people

Guiding Principle

INet will achieve results with the highest integrity, with a focus on enhancing the success of our customers, vendors and associates.

Values

We commit to these values to guide our decisions and our behaviors:

- **Teamwork**
  We promote and support a diverse, yet unified, team. We work together to meet our common goals.
- **Respect**
  We honor the rights and beliefs of our fellow associates, our customers, our shareowners, and our community. We treat others with the highest degree of dignity, equality and trust.
- **Accountability**
  We accept our individual and team responsibilities and we meet our commitments. We take responsibility for our performance in all of our decisions and actions.
- **Integrity**
  We employ the highest ethical standards, demonstrating honesty and fairness in every action that we take.
- **Innovation**
  We are creative in delivering value to our fellow associates, customers, shareowners, and community. We anticipate change and capitalize on the many opportunities that arise.

Our Strategic Focus

Our strategic focus which support and enhance our position in the IT sector is to drive profitable growth by growing and optimizing our core business and expanding at the market.

Achieve Sustainable Profitable Growth

- *We continually improve our operations* - by enhancing our capabilities while reducing costs to provide an efficient flow of products and services through the IT value chain. By optimizing delivery methodologies, we deliver faster, while reducing costs. We are also enhancing our revenues through the development of tools and capabilities to identify new growth opportunities. By streamlining our catalogue to include the products most desired by our customers, we optimize inventory management, focus on higher margin opportunities, and develop merchandising and pricing strategies that produce enhanced business results.
- *We benefit from a growth perspective by targeting market segments that provide growth opportunities for customers and vendors* - We look for opportunities to invest in high-growth and profitable geographic markets. We will continually evaluate developing markets for expansion where IT demand supports a local presence. Therefore, INet developed its business in Kosovo (Serbia and Montenegro), and filled the absence in the IT sector in that region.
- *We provide supply chain solutions* - tailored to each region to clients who are focused on increasing supply chain efficiencies, lowering overhead costs, and maximizing profits. We help our supply chain clients deliver products to key customers and new markets on a fee-for-service basis.

Optimal Productivity

- Our focus on driving efficiencies and achieving the best-in-class financial metrics has enabled us to improve our operating margins - We employ a disciplined and focused approach when we review our operations and develop initiatives designed to streamline business processes and further increase our operating efficiency.
- *By maximizing economies of scale and leveraging our best-in-class logistics services* - we are prepared to address the changing needs of resellers and suppliers, providing a broad array of distribution and supply chain management solutions, services and programs.
- *We are continuously looking for ways to take cost out of our business* - INet is taking significant actions to improve the financial position. We are always focused on finding new ways to more cost-effectively respond to market demands.

Serving Our Communities

Our Purpose

INet's Corporate Giving Program invests volunteer, cash and in-kind support in communities where our associates live and work. These investments are directed to innovative programs to promote education and economic self-sufficiency, to ensure quality of life and improve the health and well-being of citizens.
This program, guided by our corporate values of teamwork, respect, accountability, integrity and innovation, focuses on three areas:

Education

Support is targeted at scholarships, computer science, distribution management and other programs that promote economic self-sufficiency. General operating support will not be considered.

Health and Human Services

Support is targeted at community-based social and health service agencies for specific programs. A significant portion of the support granted in this area will be channeled through INet's investment. General operating support will not be considered.

Arts and Culture

Program support is targeted at performing arts centres and cultural organizations. General operating support and requests to underwrite performances and exhibitions will not be considered.

Sales and Marketing

We employ sales representatives who assist our clients with product and solution specifications, system configuration, new product/service introductions, pricing, and availability. Our product management and marketing groups also promote our sales growth, and create demand for our suppliers' products and services, and facilitate customer contact. Our product portfolio is enlarged and improved with the services that the company is offering. The product portfolio combined with IT professional services on the premier level is on of the important steps that we are planning to promote and develop. The IT products and services distribution industry is characterized by intense competition but the business plan that has been developed is that the company should establish B2B contact and collaboration in order to overrun the regional market and promote itself.
We believe that customer information systems and product ordering and delivery systems, including Internet-based systems, are becoming increasingly important in the distribution of technology products and services. Therefore the company promotes the web site with its features and capabilities in order to reduce time and costs that the employees are spending and in order the sale to become more effective. Customers can access the company's' IT system through Internet on the web site www.inet.com.mk, and also there is possibility for our partners in Macedonia and abroad to access our partner web site partner.inet.com.mk.
Our marketing programs are tailored to meet specific supplier and reseller customer needs. These needs are met through a wide offering of services by our marketing department including advertising, direct mail campaigns, market research, on-line marketing, retail programs, sales promotions, training, solutions marketing, and other events.

> *Selling Arrangements - We offer various credit terms to qualifying customers, as well as prepay, credit card, and cash on delivery terms. We also offer various alternative financing solutions to our clients based on their creditworthiness and, in some cases, the creditworthiness of their end-users, to assist our resellers and their end-users in acquiring products.*

Products

We distribute and market hundreds IT products witch our clients require and our revenue mix by product category has remained relatively stable over the past several years, although it may slightly fluctuate between and within different operating times.
INet currently offers the following products:

- IBM PC Products –xServer, Data Storage, Accessories
- Lenovo PC Products – ThinkCentre, ThinkPad, Microperipherals, Monitors, Accessories
- INetX PCs – TQM-certified assembly line
- Non-IBM PC Products - Quest PCs, Data Storage, Microperipherals, Monitors, Accessories

- Software Packages – Red Hat, SAP, Trend Micro, IBM, Microsoft
- Peripherals – Xerox printers and scanners
- Cabling / Networking Systems – Nexans / Cisco

In addition we present table for customers, orders and average orders per year, starting from year 2004 until 2007.

	2004	2005	2006	2007
Number of customers per year	565	493	435	432
Number of orders per year	2137	2168	1931	1719
Average value of order per year in EUR	775	828	824	1.356

Red Hat

Red Hat is the premier Linux and open source provider and the most recognized Linux brand in the world. They serve global enterprises through technology and services made possible by the open source model. Solutions include Red Hat Enterprise Linux operating platforms, sold through a subscription model, and a broad range of services: consulting, 24x7 support, Red Hat Network. Red Hat's global training program operates in more than 60 locations worldwide and features RHCE, the global standard Linux certification.

Red Hat is the world's most trusted provider of Linux and open source technology, the recognized leader in enterprise solutions that take full advantage of the irrepressible power of the open source model.

In addition to the agreement for INet Inc. as Red Hat Products and Services, which services create a comprehensive solution that allows enterprises to take full advantage of Linux and open source software, including all of its cost and performance advantages, the company became and **Red Hat Certified Training Partner** and in 2007 announced various Red Hat Certified Courses.

IBM SW

INet is well known in the ICT business community in Macedonia and Kosovo as one of the most reliable IBM PCD distributors since 1998. INet has a long ICT distribution history and is very familiar with all distribution administrative and operational procedures of the ICT supply chain. In 1998 the company became IBM PC Distributor for Macedonia. In 2001 INet has been accepted into IBM PartnerWorld for Software (PWSW) at the Member level, and first time consideration for INet to become an IBM SW distributor was year 2004, and during 2006 IBM SW Distribution Application was submitted. INet IBM SW Distribution Business Case was presented to the IBM Office in Belgrade and INet expects to sing an IBM SW Distribution Agreement in 2008.

Suppliers

Our suppliers generally warrant the products we distribute and allow returns of defective products, including those returned to us by our customers. We have written distribution agreements with many of our suppliers; however, these agreements usually provide for nonexclusive distribution rights and often include territorial restrictions. The agreements are also generally short term, subject to periodic renewal, and often contain provisions permitting termination by either party without cause upon relatively short notice. Our biggest suppliers are presented in the table in percentage starting from 2004 until 2007.

%	2004	2005	2006	2007
IBM	53,00	40,65	32,68	45,85
Lenovo	-	20,31	44,25	40,26
Info Quest	10,46	12,96	4,47	1,22
Others	28,62	21,11	18,60	12,67

Competition

We operate in a highly competitive environment on our domestic market and internationally. The IT products and services distribution industry is characterized by intense competition, based primarily on:

- ability to tailor specific solutions to customer needs;
- availability of technical and product information;
- credit terms and availability;
- effectiveness of sales and marketing programs;
- price;

- products and services availability;
- quality and breadth of product lines and services;
- delivery service.

We believe we compete favorably with respect to each of these factors. We compete with a variety of national and regional distributors. The evolving direct-sales relationships between suppliers, resellers, and end-users continue to introduce change into our competitive landscape. We are constantly seeking to expand our business into areas closely related to our core IT products and services distribution business.
As we enter new business areas, including value-added services, we may encounter increased competition from current competitors and/or from new competitors, some of which may be our current customers.

EU Projects

In order to become familiar with the EU standards, legislative and to be closer to the European community from the managerial perspective, INet has expanded the involvement in the EU projects supported by the governmental institutions and various EU initiatives. The company gain management skills, soft skills, sales skills and strategies of the human resources development which resulted in improved segments and areas identified as company weaknesses. This period the company will be focused on:

- 7-th Framework Programme, launched by the European Commission;
- IPA -Instrument for Pre-Accession Assistance offers rationalised assistance to countries aspiring to join the European Union on the basis of the lessons learnt from previous external assistance and pre-accession instruments;
- South East Europe Programme - aims to develop transnational partnerships on matters of strategic importance, in order to improve the territorial, economic and social integration process and to contribute to cohesion, stability and competitiveness of the region.

Cautionary Statements for Purposes of the Safe Harbour Provisions

The matters in this Report that are forward-looking statements are based on current management expectations that involve certain risks, including without limitation: intense competition; foreign exchange rate fluctuations; failure to attract new sources; failure in timely fashion to remain competitive; the potential for continued restrictive vendor terms and conditions; changes in tax rules and regulations; impact from downturn economic conditions, governmental controls and political or economic instability on domestic market; the potential decline as well as seasonal variations in demands for the company’s products and services; product supply shortages; rapid product improvement and technological change; risk of credit loss; continued pricing and margin pressures; dependency on independent shipping companies.

INet has instituted and continues to institute changes to its strategies, operations and processes to address these risk factors to mitigate their impact on the company’s results of operations and financial condition. However, no assurance can be given that the company will be successful in these efforts.

Community Relations

Global Compact – Communication on Progress

INet Inc. is among the first Macedonian companies that joined Global Compact initiative in January 2005, embracing and supporting the ten universal principles of corporate social responsibility as part of its operations. As Global Compact participant INet Inc. has shown excellence in promoting and integrating the ten principles into overall company strategy:

- respect and protection of human rights;
- respect of labour rights and fighting against workers abuse, especially against the abuse of children;
- environment protection and development of "friendly" technologies;
- fighting against any kind of corruption, including bribe and extortion;

International human right is not just responsibility of governments but every individual and every organ of the society has obligation to respect and promote the human rights. INet Inc. has taken particular care to ensure that its activities and practices do not contravene international human rights low. All contracts with partners and suppliers are and are going to be in compliance with human rights. Partnership activities based on equity, transparency and mutual benefit are and will be subject of future relationship. INet Inc. has implemented policies addressing corporate social responsibility, health and safety non-discrimination working environment. INet aligns its behaviour with the expectation of their stakeholders. INet Inc. has participated on the Regional Corporate Social Responsibility (CSR) Conference for businesses and stakeholders “CSR in New Europe” in Brussels in

June 2007, in order to exchange information and good practices and promotion of multi-stakeholder dialogue among businesses, governments, academia and civil society representatives, with a view of encouraging discussion on What, Why, When and How could be done in the New Europe to accelerate CSR.
INet Inc. believes that dynamic which results from freedom of association can sat in motion ‘decent work – cycle’ through constructive dialogue that harnesses energy to focus on solutions and that results in benefits to the enterprise, its stakeholders and society at a large. Forced labour deprives societies of the opportunity to develop human resources for the modern labour market and to develop skills and educate children for the labour markets of tomorrow. Discrimination affects the individuals concerned and negatively influences the greater contribution that they might make to society. Having considered all this INet Inc. will continue to improve its policies, educate its employees and foster open dialog with its stakeholders concerning labour rights.
INet Inc., extends its commitment to corporate citizenship and social responsibility throughout the company. Whether we are conserving energy and natural resources, ensuring a safe and healthful workplace, or working with our suppliers to develop sustainable global markets, we apply our extensive innovation resources and expertise to solve some of the most pressing global issues.
The nine principles need to be strengthened by a strong stance against corruption. Corruption weakens economic growth and social development, the consolidation of democracy and people’s morality. INet Inc. is committed to conducting business in a fair, honest and sound manner to help assure that the long term interests of its shareholders are being served. As part of this commitment, Code of Conduct was developed which sets out the policies and procedures for the fair and honest business practices and behaviour that INet Inc. expects from its staff.

Corporate Social Responsibility (CSR)

In November 2006, in coordination with Institute for Sustainable Communities (ISC), Civil Society Strengthening Project, Skopje, INet has started the initial activities about CSR focused on:

- collaboration among INet Inc. and NGOs for further references and progress in Social Responsibility
- working environment improvement and respect of labour principles

Impulse of INet Social Responsibility is directed within the company, in a way of improving working atmosphere and supporting of specific social fulfillment, as it may be also affective on our business partners.
The activities continued in 2007 with meetings with NGO’s, as an opportunity to partner with ISC on some initiatives that will be of mutual benefit to our company and the NGO’s in Macedonia.

Corporate Governance

Corporate Governance is a part of the corporate strategy of INet. The company has started a project setting a basis for improved corporate governance in the Company. The project started in September, 2006 with Cooperation Agreement between INet Inc. and IFC (International Finance Corporation).
IFC, a member of the World Bank Group, is an international organization whose mission is to promote sustainable private sector investment in developing countries, helping to reduce poverty and improve people’s live. The IFC project’s goal is to improve Corporate Governance standards in South East Europe.
The value of Integrity of INet states: "We employ the highest ethical standards, demonstrating honesty and fairness in every action that we take". Just as important is our value of Accountability, that: "we take responsibility for our performance in all of our decisions and actions". Building upon these values and upon long-standing Company policies of legal and ethical compliance, through this intervention the Company reaffirmed the commitment to the highest standards of legal and ethical conduct. As a result of this effective IFC assistance, a very solid foundation should be established for INet to improve its corporate governance practices. The project has been successfully finished in June 2007.
Since the fact that INet is a Joint Stock Company, the Communication Strategy with its stakeholders is defined in a way that all information must be transparent – the report of the activities taken to be presented in the Annual Report of INet, a document which is public and is located on our web site www.inet.com.mk.

Employees Benefits

INet is an employer that is providing its employees with a benefit program responsive both to the diversity of its community and to the many life changes individuals experience during their employment. Qualified employees are eligible for the majority of benefits immediately upon hire.

INet contributes a significant amount of benefits, such as:

Auspicious working time - guided from the idea that working time could improve working atmosphere and support specific social fulfillment to its employees.

Collective worker's insurance - our life, health and body integrity can not be stated in money. Because of INet's care for the security of its employees and their families, every year all of them are collectively insured in one of the best Macedonian insurance companies.

Dental care - INet, on behalf of its employees has concluded a contract with Dental Clinical Center as highest institution in dental area in Republic of Macedonia. All services provided by this dental clinical centre can be used by INet's employees and their closest family.

Medical examinations of workers – according to the Work Protection Low, the company organizes medical examinations of workers once a year.

Compensation for overtime work - in order to complete duties on time, and in some other cases, employees could extend working time. This is defined with procedure for overtime compensation, which means that extension is followed and evaluated by managers, and is compensated according to the Working Relations Low.

Mobile phones – by the end of 2007 six (6) most qualified employees are given the opportunity to use paid mobile lines and phones. In the near future INet Inc. plans to give this opportunity to all employees.

Possibility to purchase goods from many different stores under special conditions - In the few stores for technical equipment, our employees can buy products under special conditions such as: reduced prices and delayed payment without additional costs up to 6 months.

Possibility to purchase products from INet's assortment with special price reduction - All products that INet offers from its own product portfolio can be purchased by employees with reduced price on lowest possible level.

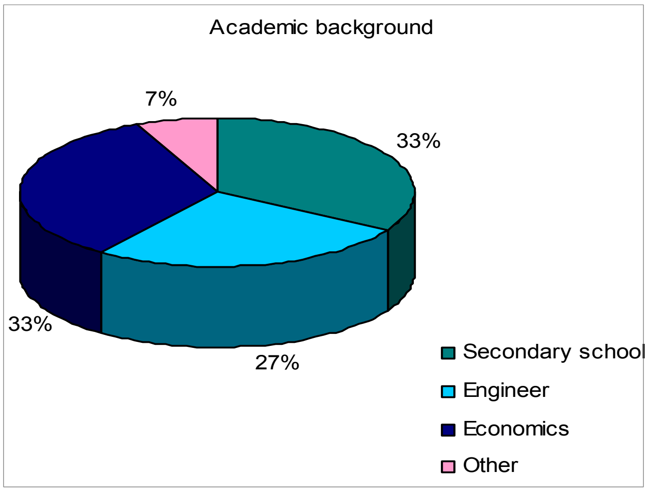
Insurance broker services - INet has signed agreement with an Insurance Broker house. All services provided, can be used by employees too, again, under special conditions like delayed payment without additional expenses, or special discount for cash payment.

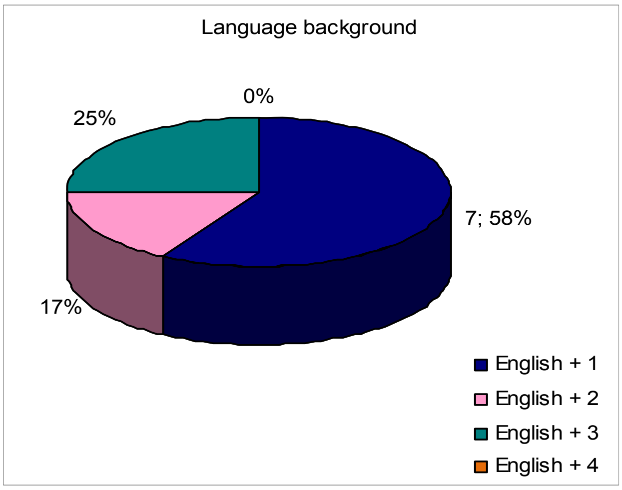
Trainings - Taking care of its own employee skills, facilities and professionalism, in accordance to the innovations and in order the employees to get improvement wherever it is possible and needed, they have chance to attend at different courses and trainings and afterwards to get additional skills useful in everyday activities.

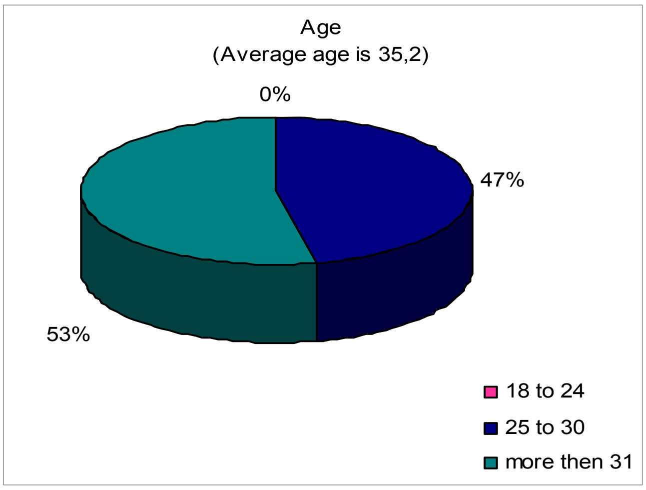
Purchasing goods in Markets with delayed payment - Many years ago INet has concluded agreement with Markets, which means that employees could purchase goods from their markets with special membership cards, up to the previous defined limit, and pay off days later.

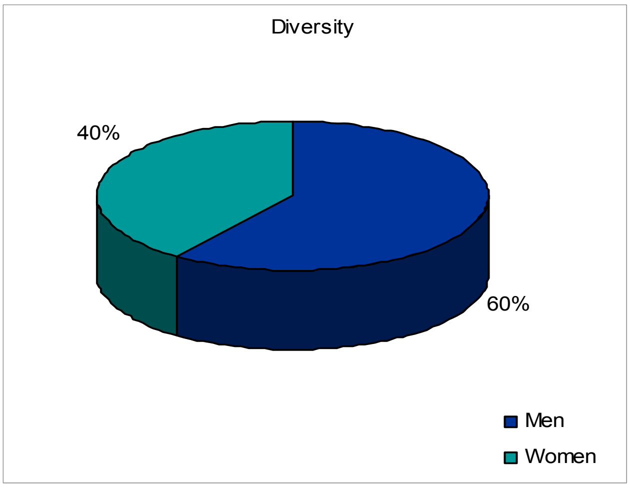
Occasional gifts - INet's yearly budget includes designate sum that could be used for occasional gifts. That means that every celebration connected to employees, like: birthday, wedding, new born child, name day, etc. is noted and rewarded with occasional gift.

INet Employees









Commitment to quality

January, 2007 INet Inc. had been awarded with IT Mark Certificate. The Appraisal was conducted by ESI (European Software Institute) Centre, Bulgaria.

Being distinctively better than rivals on one or more Key Success Factors (KSFs) presents a golden opportunity for gaining competitive advantage. A key factor to our success today and in a future is a strategy that helps INet to run the business more effectively. One of the best practices that INet choose between accepted internal **Quality Methodologies** is IT Mark certification – CMMI quality certification.

In general, IT Mark assesses and certifies the quality of SMEs in three main areas: one related to overall **Business Management** (strategic, commercial, financial, marketing, etc); another on **Information Security Management**; and the third one, specifically related to the Maturity of their **Software & Systems Processes**. In matters relating to Business Management the reference used is the **10-Squared model**, which was developed to assess applications for Venture Capital. From the Information Security Management point of view, the reference model is the **ISO 17799**, whereas for Software & Systems a lightweight version of **CMMI®** is used, a standard globally acknowledged by the IT world with which ESI has broad experience in providing services to enterprises in all five continents.

In the future, INet will continue to follow existing quality standard processes & procedures, and will intend to be certified by different international rules and regulations. In the mean time, INet insists to achieve the best possible quality and certification, in order to ensure that businesses succeed.

SELECTED FINANCIAL DATA

The following table presents selected financial data of INet Inc. (“INet” or the “company”). The information set forth should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and the historical financial statements.
References below to 2005, 2006 and 2007 represent the fiscal years of INet as a 52- or 53-week period ending on December 31.

Fiscal Year Euro (€)	***2005***	***2006***	***2007***
Selected Operating Info (1 EUR = Den. as of 31.12)	***61.1779***	***61.1741***	***61.2016***
Net Sales	1.795.851	1.552.698	2.473.691
Gross profit	344.057	351.576	520.164
Income before income taxes	53.389	6.667	68.323
Net income	45.297	2.182	53.312
Common Shares Outstanding	13.844	13.844	13.844
Selected Balance Sheet Info			
Cash and cash equivalents	83.501	62.554	95.939
Total assets	385.083	561.402	602.264
Total liabilities	248.489	422.659	410.271
Stockholder’s equity	136.594	138.743	191.992

The following table sets the percentage of total net sales company’s represented thereby, for each of the fiscal years indicate:

Percentage of Net Sales	***2005***	***2006***	***2007***
Net Sales	100%	100%	100%
Cost of goods sold	80.85	77.36	78,97
Gross profit	19.15	22.64	21,03
Operating expenses: - S&M expenses - R&D expenses - G&A expenses	17.10	23.10	19,99
Other (income) expense	0.02	0.01	0,00
Net income before taxes	2.97	0.43	2,76
Taxes	0.45	0.29	0,61
Net income	2.52	0.14	2,16

The company net sales increase to €2.47 million in 2007 from €1.55 million in 2006.
Gross margin is relatively stable with intention to grow in the future as the result of the modifying pricing policies and term and conditions for our customers. As we may experience negative sales growth of changing these terms, INet must remain in the stable limit, terms and conditions.
Other (income) expense consisted primarily of interest, foreign currency exchange losses, and fees associated with the company’s accounts receivable facilities. The table is showing tendencies during previous years.

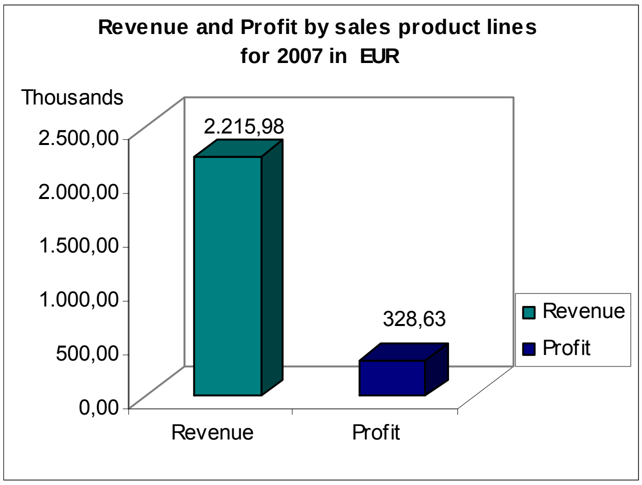
Revenue and Profit by Departments in EUR

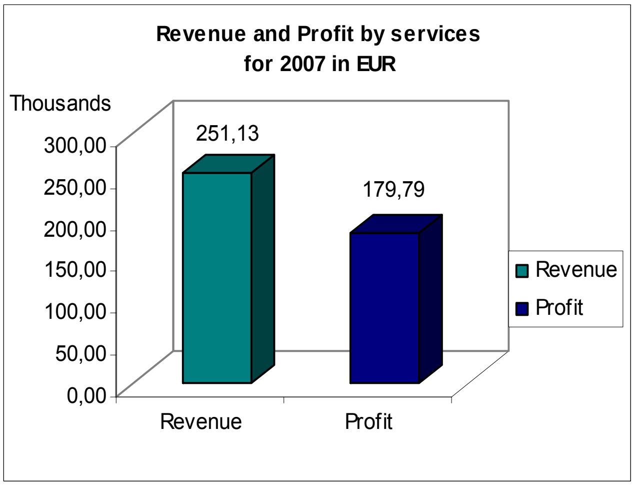
The following pie charts present our data about revenue and profit by the three departments of INet:

- ***INet Sales Department*** – to service small and medium size corporations as well as the retail market through an extensive network of dealers:
    - Representation & Distribution of ICT products (IBM, Lenovo, SAP, Red Hat products etc.)

- INetX PC Integration Center – based on Info-Quest distribution products
- INet Financial Services – flexible financing options to help consumer market and qualified customers keep costs down and PCs current.

- ***INet Customer Support Department:***
  - Red Hat Linux Solutions
  - Trend Micro Antivirus Products & Solutions
  - INet Service Level Agreements – long-term contracts for comprehensive setup, network structure optimization & security, system upgrades & migrations, help desk support and maintenance.
  - INet Support Services – for comprehensive setup, help desk support and maintenance:
    - INet SLA Help Desk Support
    - INet Product Installation Services
    - INet Product Maintenance Services
    - INet Cabling & Wireless Solutions Services - offering the best cabling and wireless infrastructure
- ***INet Center of Excellence*** – in order to service corporations of all sizes for a fast implementation of ICT solutions:
  - Consulting Services – SAP implementation and consulting, ICT strategy developments, ICT business assessment, BPR, IBM & Lotus based e-Business & e-Government solutions
  - Education Services – IBM Training Courses, Red Hat Training
  - Participating in EU projects





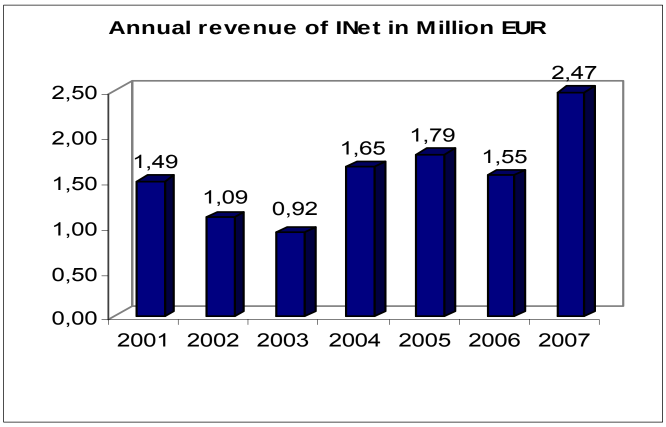
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

Sales

INet is one of the leading distributors of IT products and services on the domestic and neighboring markets. We offer range of IT products, services and education and help generate demand and create efficiencies for our customers and suppliers. The company generated annual sales from existing operations, addition of new vendors and product categories, new customers, increased sales to some existing customer base, reducing the costs etc. The company's net sales increased to €2.47 million in 2007.

Net sales was primarily attributable to big demand for technology products in the public sector and projects that were on a national level. In addition, during 2007, the demand for information technology products and services was becoming stronger and bigger and the addition of new customers (government, public organizations, primary and secondary schools), increased sales to the existing customer base, and expansion of the company's product and service offerings.

If we analyze the period of existing and working of one decade of INet, we can see the chart which shows results of annual revenue for period 2001-2007.



Gross Margin

The IT distribution industry in which we operate is characterized by narrow gross profit as a percentage of net sales (""gross margin") and narrow income from operations as a percentage of net sales ("operating margin"). The margins have been negatively impacted by intense price competition, as well as changes in vendor terms and conditions, including, but not limited to, significant reductions in vendor rebates and incentives, tighter restrictions on our ability to return inventory to vendors, and reduced time periods qualifying for price protection. To mitigate and reduce these factors, we have implemented, and continue to refine, changes to our pricing strategies, inventory management processes, and vendor program processes. In addition, we continuously monitor and change, as appropriate, certain of the terms and conditions offered to our customers to reflect those being set by our vendors.

Critical Accounting Policies and Estimates

The discussions and analyses of our financial condition and results of operation were based on our financial statements, which have been prepared in conformity with International Accounting Standards. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of any contingent assets and liabilities at the financial statement date, and reported amounts of revenue and expenses during the reporting period. On an ongoing basis, we review and evaluate our estimates and assumptions, including those that relate to accounts receivable, vendor programs, inventories, goodwill, intangible assets and other long-lived assets, income taxes, and contingencies and litigations.

Our estimates are based on our historical experience and a variety of other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making our judgment about the

carrying values of assets and liabilities are not readily available from other sources. Actual result could differ from these estimates under different assumptions or conditions.
We believe the following critical accounting policies are affected by our judgment, estimates and/or assumptions used in the preparation of our financial statements.

- *Account Receivable* – Having receivables means that the company has made the sale but has yet to collect the money from the purchaser. We provide allowances for doubtful accounts on our accounts receivable, including retained interest in securitized receivables, for estimated losses resulting from the inability of our customers to make required payments. Changes in the financial condition of our customers or other unanticipated events, which may affect their ability to make payments, could result in were to deteriorate, which may result in the impairment of their ability to make payments, additional allowances may be required. Our estimates are influenced by the following considerations: the small number of customers, the fact that one customer accounts for 50% or more of our net sales, the non-standard credit evaluation of our customer's financial condition, our credit non-insurance coverage and non-collateral requirements from our customers in certain circumstances.
- *Vendor Programs* – We receive funds from vendors (IBM, Lenovo) for price protection, product rebates, marketing and training, and promotion programs which are generally recorded, net of direct costs, as adjustments to product costs, revenue, or selling, general and administrative expenses according to the nature of the program. Some of these programs may extend over one or more quarterly reporting periods. We accrue rebates or other vendor incentives as earned based on sales of qualifying products or as services are provided in accordance with the terms of the related program. Actual rebates may vary based on volume or other sales achievement levels, which could result in an increase or reduction in the estimated amounts previously accrued. We also provide reserves for receivables on vendor programs for estimated losses resulting from vendors' inability to pay, or rejections of claims by vendors.
- *Inventories* – Our inventory levels are based on our projections of future demand and market conditions. Any sudden decline in demand and/or rapid product improvements and technological changes could cause us to have excess and/or obsolete inventories. On an ongoing basis, we review for estimated excess or obsolete inventories and write down our inventories to their estimated net realizable value based upon our forecasts of future demand and market conditions. If actual market conditions are less favorable than our forecasts, additional inventory reserves may be required. Our estimates are influenced by the following considerations: sudden decline in demand due to economic downturn, rapid product improvements and technological changes, our ability to return to vendors a certain percentage of our purchases, and protection from loss in value of inventory under our vendor agreements.
- *Goodwill, Intangible Assets and Other Long-Lived Assets* – We asses potential impairment of goodwill, intangible assets and other long-lived assets when there is evidence that recent events or changes in circumstances have made recovery of an asset's carrying value unlikely. When the sum of the expected, undiscounted future net cash flows is less than the carrying value of an asset, an impairment loss will be recognized. The amount of an impairment loss would be recognized as the excess of the asset's carrying value over its fair value. Factors we consider important, which may cause impairment include: significant changes in the manner of use of the acquired asset, negative industry or economic trends, and significant underperformance relative to historical or projected future operating results. In accordance with the International Accounting Standards, we will not amortize goodwill or indefinite-lived intangible assets and these assets will be reviewed for impairment at least annually.
- *Income Taxes* – As part of the process of preparing our financial statements, we have to estimate our income taxes in each of the taxing jurisdictions in which we operate. This process involves estimating our actual current tax expense together with assessing any temporary differences resulting from the different treatment of certain items, such as the timing for recognizing revenues and expenses, for tax and accounting purposes. We are required to asses the likelihood that our deferred tax assets, which include net operating loss carry forwards and temporary differences that are expected to be deductible in future years, will be recoverable from future taxable income or other tax planning strategies. If recovery is not likely, we have to provide a valuation allowance based on our estimates of future taxable income in the various taxing jurisdictions, and the amount of deferred taxes that are ultimately realizable. The provision for current ad deferred tax liabilities involves evaluations and judgments of uncertainties in the interpretation of complex tax regulations by various taxing authorities.

- *Contingencies and Litigations* – There might be various claims, lawsuits and pending actions against us incident to our operations. If a loss arising from these actions is probable and can be reasonably estimated, we record the amount of the loss. Based on current available information, we believe that the ultimate resolution of these actions will not have a material adverse effect on our financial statements. As additional information becomes available, we assess any potential liability related to these actions and may need to revise our estimates. Future revisions of our estimates could materially impact the results of our operations and financial position.

Quarterly Data, Seasonality

INet's quarterly operating results have fluctuated significantly in the past and will likely continue to do so in the future as a result of: seasonal variations in the demand for the products and services such as lower demand during the summer months and pre-holiday stocking in the retail channel; competitive conditions in our industry, which may impact the prices charged and terms and conditions imposed by our suppliers and/or competitors and the prices or terms and conditions we offer our customers, which in turn may negatively impact our revenues and/or gross margins; currency fluctuations; variation in the amount of provisions for excess and obsolete inventory, vendor sponsored programs, and doubtful accounts resulting from technological changes or other changes in the market or e whole; changes in the level of operating expenses; the introduction by suppliers of new hardware and software products and services which may result in the obsolescence of existing products and/or affect the mix of products sold or overall demand; the loss or consolidation of a significant supplier or customer; product supply constraints; interest rate fluctuations and general economic conditions**.**

Liquidity and Capital Resources

Cash flows

We have enhanced its growth and cash needs largely through income from operations, short-term borrowings, credit and other facilities, collecting of accounts receivable, and trade and supplier credit.
In 2007 the objective of the company has been to improve the utilization of working capital and put assets to work through increasing inventory turns and steady management of vendor payables and customer receivables. INet will continue to strive for further improvements in working capital management and debt reduction for the foreseeable future.
Our cash and cash equivalents totaled 96€ thousands in 2007.

Capital resources

Starting from 2003 and until the end of the 2007 the company had 10 Loan Agreements with Crimson Capital provided for working capital and investments. They resulted with financial growth trend with intention to continue in next years.

Crimson Capital – Loan Agreements:

- From 07.11.2003 to 16.01.2004, (Pilot project 1) - 45.700,00 USD for Working capital;
- From 27.01.2004 to 20.12.2004, (Project 2 and 3) – 2 x 100.000,00 USD for Working capital;
- From 13.01.2005 to 15.06.2005 (Project 4) – 100.000,00 USD for Investments and Working capital;
- From 05.07.2005 to 25.11.2005 (Project 5) – 100.000,00 USD for Investments and Working capital;
- From 28.11.2005 to 30.05.2006 (Project 6) – 120.000,00 USD for Investments and Working capital;
- From 12.06.2006 to 31.12.2006 (Project 7) – 120.000,00 USD for Investments and Working capital;
- From 20.12.2006 to 21.08.2007 (Project 8) – 120.000,00 USD for Investments and Working capital;
- From 21.08.2007 to 22.02.2008 (Project 9) – 100.000,00 USD for Investments and Working capital;
- From 29.02.2008 to 03.03.2009 (Project 10) – 120.000,00 USD for Investments and Working capital;

INet believes that existing cash resources and cash provided by operating activities, supplemented as necessary with funds available under credit arrangements will provide sufficient resources to meet its present and future working capital and cash requirements.

Market risk

We are exposed to the impact of the foreign currency fluctuations and interest rate changes. In the normal course of business, INet is unable to employ established policies and procedures to manage its exposure to fluctuations in the value of the foreign currencies and interest rates using a variety of financial instruments. It is the our policy to utilize financial instruments in a future to reduce risks, but not to enter into foreign currency or interest rate transactions for speculative purposes.

In addition to product sales and costs, the company has foreign currency risk related to debt that is denominated in local currency. The company's foreign currency risk management objective is to protect its earnings and cash flows resulting from sales, purchases and other transactions from the adverse impact of exchange rate movements.

We are exposed to changes in interest rates primarily as a result of our short-term debt used to maintain liquidity and finance inventory, capital expenditures and business expansion. The company's interest rate risk management objective is to limit the impact of interest rate changes on earnings and cash flows and to lower its overall borrowing costs.

Market risk management

Foreign exchange and interest rate risk should be monitored in a future using a variety of techniques including a review of market value, sensitivity analysis and Value-at-Risk techniques. ("VAR"). The VAR model determines the maximum potential loss in the fair value of foreign exchange rate sensitive financial instruments assuming a one-day holding period. The VAR model estimates should be made assuming normal market conditions and 95% confidence level.

Euro conversion

Beginning in January 1, 2002, the company has implemented plans to address the issues raised by the euro currency conversion. The company's Built-to-Run ERP computer information systems and ISO-9000:2000 business processes and equipment generally accommodate multiple currencies and euro-denominated transactions.

FINANCIAL STATEMENTS AND SUPLEMENTARY DATA

Balance Sheet

ASSETS	***Amount in EUR***	
	2006	***2007***
A. The requests for the inscribed, but not paid capital	**0**	**0**
B. Fixed assets	**100.638**	**125.634**
Non- material assets	616	0
Material assets	84.820	121.131
Financial investments	15.202	4.503
C. Current assets	**460.763**	**476.630**
Inventories - stocks	125.700	178.141
Accounts receivable - debtors	272.509	202.550
Marketable securities – short – term investments	0	0
Cash and cash equivalents	62.554	95.939
D. Prepaid expenses	**0**	**0**
E. Assets	**561.401**	**602.264**
LIABILITIES AND STOCKHOLDERS' EQUITY		
A. Capital and reserves	**138.743**	
Capital –shareholder's capital	69.187	69.156
Paid – in capital	0	0
Revaluation reserve	8.744	18
Mandatory reserve	16.392	16.384
Accumulated profit	42.565	53.123
Transferred loss (-)	0	0
The profit for the financial year	1.855	53.312
VIII. The loss for the financial year	0	0
B. Long term reservation for risks and expenses	**0**	**0**
C. Long and short – term liabilities	**422.658**	**410.271**
D. Delayed payment of expenses and revenues in total period	**0**	**0**
E. Liabilities and stockholders' equity	**561.401**	**602.264**

Income Statement

REVENUES	***Amount in EUR***	
	2006	***2007***
Sales revenue	1.552.698	2.473.691
Other incomes	13.547	42.472
Extraordinary incomes	161	101
Total	**1.566.406**	**2.516.264**
EXPENSES		
Operating expenses	1.520.791	2.394.655
Cost of good sold	56.846	56.846
The expenses for the employees	59.728	68.019
Net salaries	33.193	41.674
Salary expense	26.535	26.345
Depreciation	0	0
Other expenses	38.948	53.287
Extraordinary expenses	0	0
Total	**1.559.739**	**2.447.942**
FINANCIAL RESULT		
Net profits before taxes	6.667	68.322
Net losses before taxes	0	0
Taxes	4.484	15.011
Net profits after taxes	2.183	53.311
Net losses after taxes	0	0

FINANCIAL STATEMENTS ANALYSIS

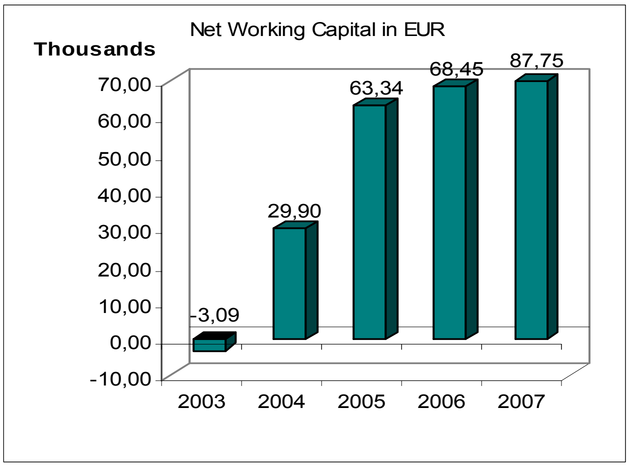
The company is using the following two analysis standards of comparison of the financial measures over a period of time:

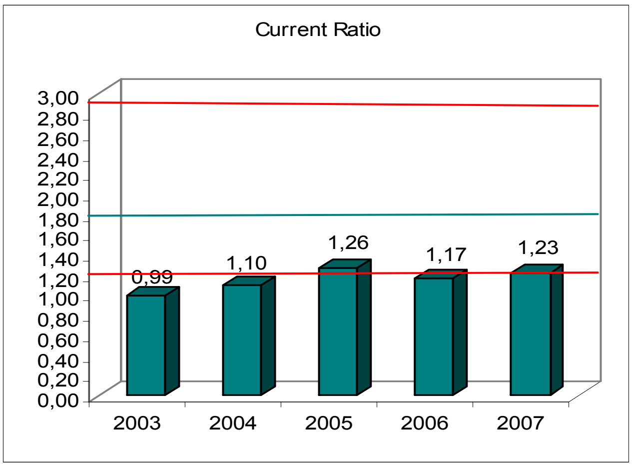
- Percentage Analysis - Horizontal and Vertical Analysis of the past performance measurements of the company;
- Comprehensive Ratio Analysis - Evaluating Liquidity, Profitability, Long-term Solvency, Cash Flow Adequacy, Market Strength.

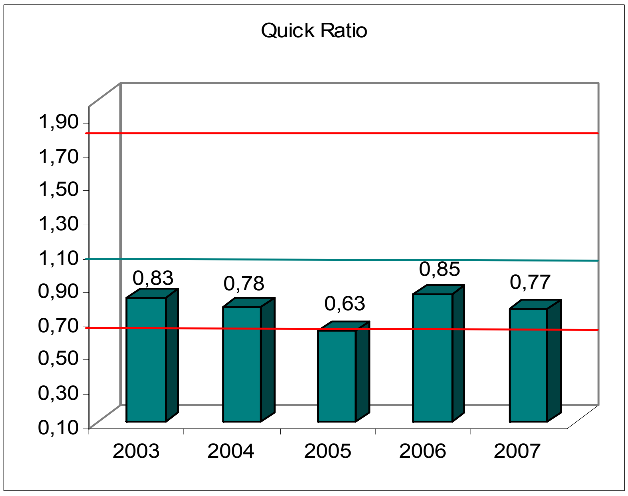
Percentage Analysis

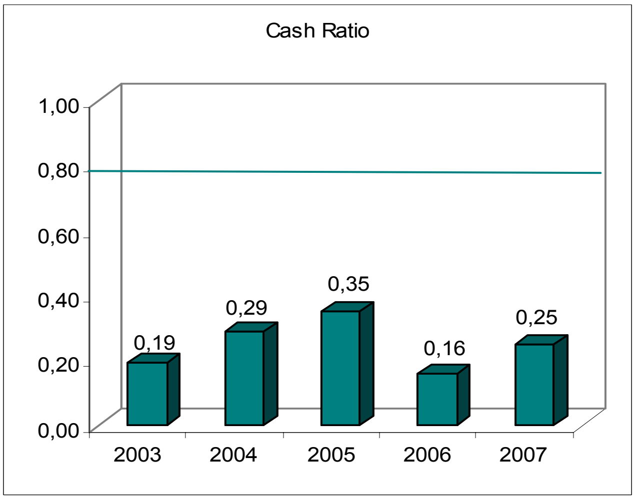
Horizontal and Vertical Analysis – Comparative Statements

Percentage analysis of the income statement focuses in the gross profit, expenses, and net income related to the gross sales. As sales grow or decline over the years, the expenses also grow or decline, which makes a direct euro-to-euro comparison impractical. However, the expenses remain relatively stable as a percentage of sales.
Percentage comparison is also done on the balance sheet to see how each item relates to the total assets. To calculate the balance sheet percentages, the individual accounts, including the liability and equity accounts, are divided by the total assets figure. In such a case the company's performance are compared to the historical performance and to the IT industry averages.
The horizontal comparison and common-size statements (vertical analysis) are explained above in this Report in the part "Management discussion and analysis". The management will use the common-size statements in the future to analyze the operating and financing characteristics of the company with other companies of same or different size in the same IT industry.
INet is using the ratio analyses which are reports for the solvency of the company, to compare the financial results in the previous years or with other companies in the industry, and to point out areas needing further investigation.
The company is using Dun & Bradstreet "Industry Norms and Key Business Ratios" industry norms for comparison. According to the reports that INet is preparing on yearly, monthly and daily base, there are ratios who gives clear picture for the INet's solvency and any ratio is maintained at a specific value as part of a financing agreement and is calculated and monitored on a timely basis. Ratio Analysis enables to spot trends in a business and to compare its performance and condition. To do this we compare our ratios with the industry averages and watching, especially for any unfavorable trends that may be starting. Ratio analysis may provide the all-important early warning indications that allow solving the business problems before business is destroyed by them. Industry averages can be used only as a broad guideline to compare the company's performance.
Indicators of liquidity - are measured by the ability of the company to satisfy its short term liabilities as they come due. It refers to the company's overall financial position.









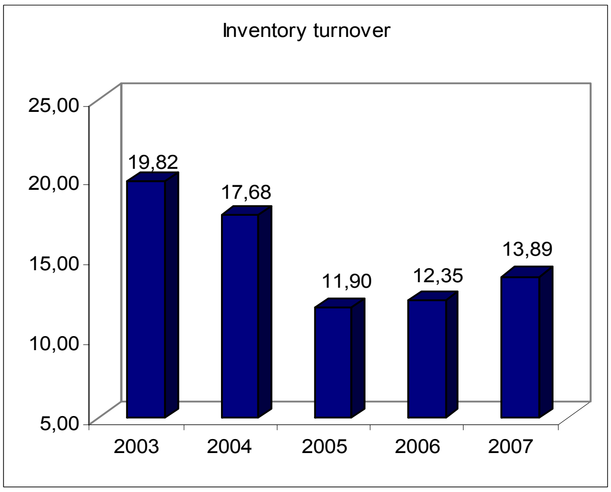
Net working capital is more a measure of cash flow than a ratio. Over the period that has been analyzed, net working capital is constantly growing which is a result of the intention for reasonable growth and stable trend according to the company growth policy.

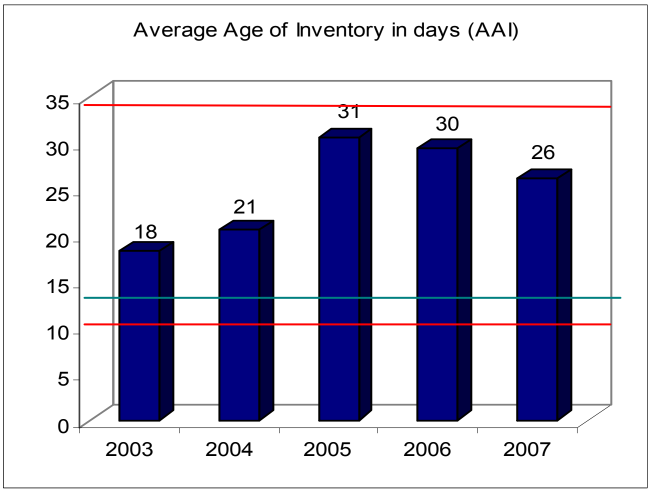
The current ratio (CUR) method is a model for measuring the liquidity and it is an indicator of a company's ability to pay short - term obligations. During the past years, the indicator was stable. In year 2007, this indicator increased at 1.23.

Quick (Acid – Test) Ratio (QUR) as an indicator of the extent to witch the company can pay current liabilities without to rely on the sale of inventory, and decreased slightly in 2007.

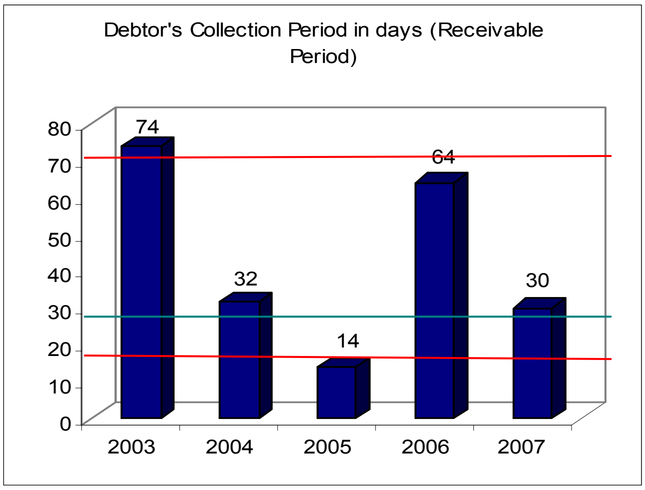
Cash ratio- measures the ability quickly to liquidate the assets and cover short - term liabilities. The cash ratio in 2007 is 0.25.

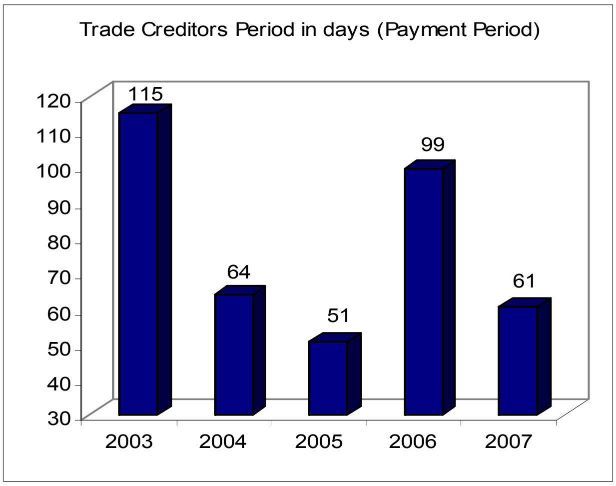
Activity ratios - measures the speed with which accounts are converted into sales or cash. This ratio indicates that INet is in a good shape and the industry averages have been reached.





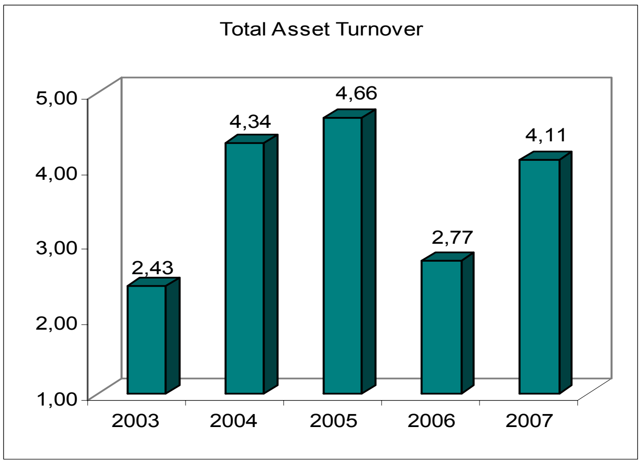
Inventory turnover - is in the frame of industry average. Also Average age of inventory decreased from 30 to 26 days on 2007. The activity ratios are stable and in the predefined industry limits and reflect good relative inventory levels of the company.

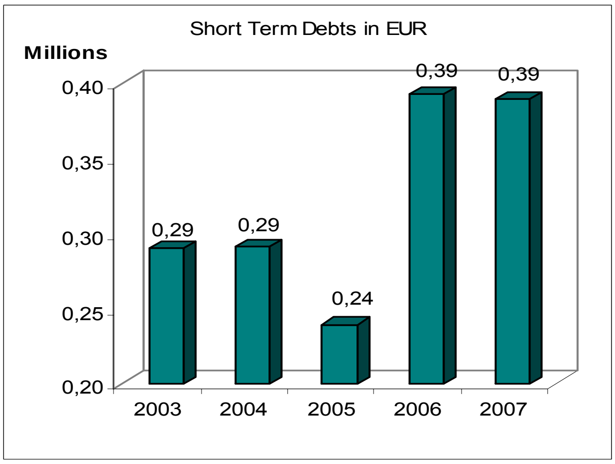


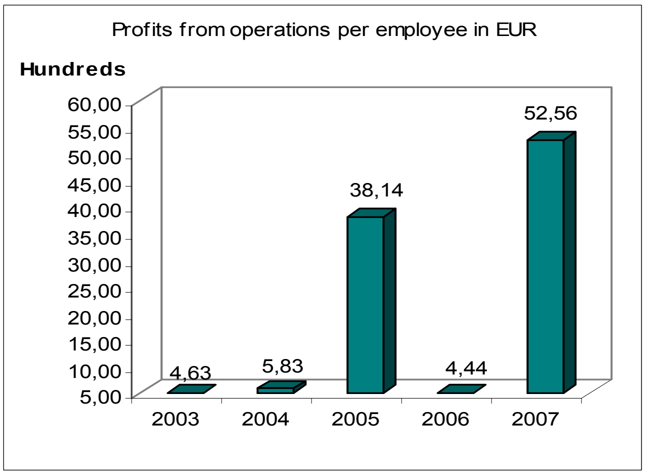


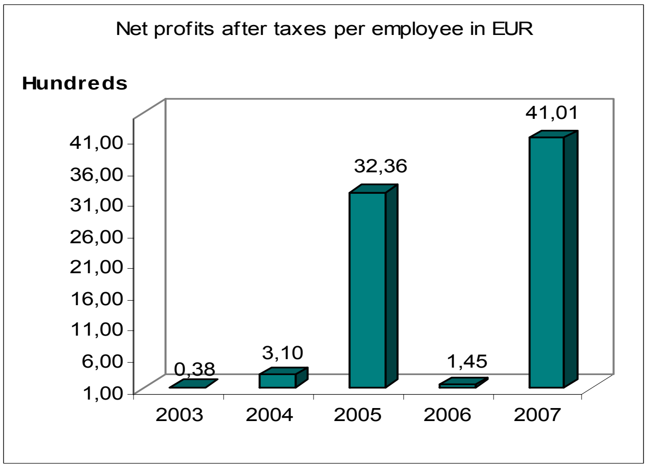
Average collection period (ACP) decreased from 64 to 30 days in 2007 and Average payment period (APP) decreased in 2007 from 99 to 61 days, witch means that INet is collecting the account receivable for shorter time, pays its bills in shorter time then previous years and reflects good success of company's credit and collection policies. Although overall liquidity appears good, some attention should be given to accounts receivable and accounts payable, even they are in the industry frame and are satisfactory. Still is in the best interest of the company to collect and pay in very short time and to have complete influence on the entire cash flow and outflow process.

Indicators of productivity, efficiency and operating - in addition there are *Total asset turnover*, *Short term debts* and also data about *Profits from operations* and *Net profits after taxes per employee* from 2003 to 2007. Total assets turnover indicate that INet has efficiency witch is on approximate high level. The company's operations have been financially efficient. Short term debts are on same level as in 2006.

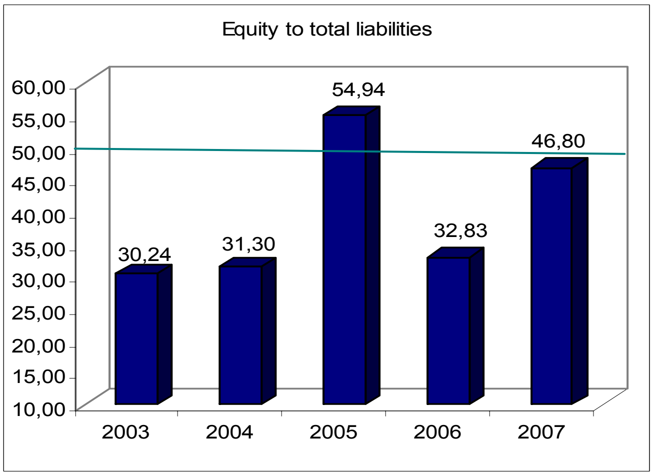


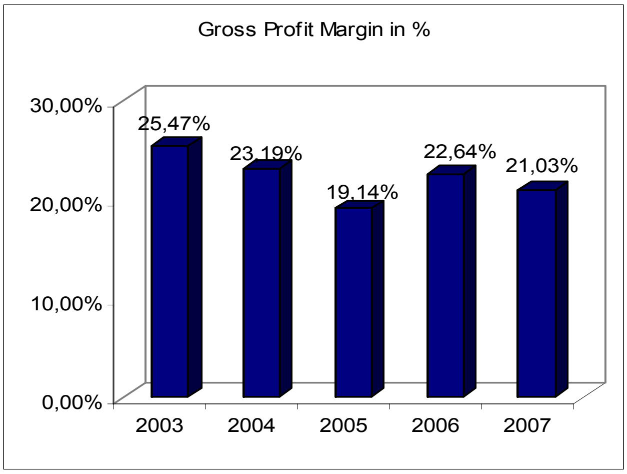






Financial leverage – is the magnification of risk and return of its debt in relation to total assets. The higher the financial leverage the more the company is considered risky. As for most ratios, an acceptable level is determined by its comparison to ratios of companies in the same industry and industry averages.





The gross profit margin ratio tells us the profit a business makes on its cost of sales, or cost of goods sold. It is a very simple idea and it tells us how much gross profit per 1€ of turnover our business is earning. Annual gross profit for 2008 is projected to be higher with while keeping the operation expenses at the same or minor level. The gross margin is not an exact estimate of the company's pricing strategy but it does give a good indication of financial health. Without an adequate gross margin, a company will be unable to pay its operating and other expenses and build for the future. The margin is stable during these years, and we have implemented and continue to refine changes to our pricing strategies, inventory management processes, and administration of vendor subsidized programs.

NOTES TO FINANCIAL STATEMENTS

Note 1 Organization and Basis of Presentation

INet Inc. (the "company" or "INet") is a privately owned entrepreneurial-based company involved in sales, rental and services of personal computers and IT based business solutions, IT education and consulting.

Note 2 Significant Accounting Policies

Fiscal year

INet financial statements are prepared for the calendar year, as a company fiscal year. All references represent the 52-week fiscal year ended December 31.

Use of Estimates

The financial statements have been made in accordance with the requirements of the regulation generally accepted in the RoM, as well as the usual accounting practice. The domestic accounting regulation differs in some aspects from the International Accounting Standards.
Preparation of financial statements in conformity with International Accounting Standards requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the financial statement date, and reported amounts of revenue and expenses during the reporting period.
These accounting policies are used consequently from year to year during a longer period of time.
INet classification rules are: INet has developed Accounts and Chart of Accounts for its own needs, with seven digits in the account numbers and hundreds of accounts in the chart of accounts.

Revenue and Expenses Recognition

INet generally recognizes sales and revenues on hardware and software products sales at the time of shipment to the customer. Service revenues are not recognized over the contractual period but upon delivery of the services, i.e. as the services are provided and performed.
The expenses are assigned to the accounting period in which they are used to produce revenue. Revenues and expenses are shown in the following categories:

- Sales – Cost of Goods Sold = Gross Profit
- Gross Profit – Operating Expenses = Income from Operations
- Income from Operations + Interest Income – Interest Expense – Taxes = Net Income After Taxes

Vendor Programs

Funds received from vendors for price protection, product rebates, marketing or training programs are recorded net of direct costs as adjustments to: cost of goods sold; selling, general and administrative expenses; or revenue according to the nature of the program.

Warranties

INet's suppliers generally warrant the products distributed by the company and allow returns of defective products, including those that have been returned to the company by its customers, The company does not independently warrant the products it distributes. However, INet does warrant the following: (1) its services with regard to products that it configures for its customers, and (2) products that it builds to order from components purchased from other sources.

Foreign Currency Translation (current rate) and Remeasurement

All foreign-currency-denominated liabilities are converted into local currency values using the exchange rate prevailing at the fiscal year ending date (the current rate).

Cost value of financial instruments

The carrying amounts of cash, accounts receivable, accounts payable and other accrued expenses approximate cost value because of the short maturity of these items. The carrying amounts of outstanding debt issued pursuant to bank credit agreements approximate cost value.

Cash
The company considers all highly liquid investments with original maturities of three months or less to be cash equivalents.
The cash and cash equivalents consist of cash on hand, bank balances and foreign exchange accounts. INet does not have any limitation regarding free disposal with the cash.

Inventories
INet is pricing inventory at cost under the *perpetual merchandise inventory system* according to the first-in, first-out (FIFO) method, as more effective for providing information about quantities and ensuring optimal customer service.

Property and Equipment
Property and equipment are recorded at cost and depreciated using the straight-line method over the useful lives estimated according to the domestic officially announced depreciation rate. The calculation is made for each asset separately (not on group of assets).

Long-Lived Assets
INet assesses potential impairments to its long-lived and intangible assets when there is evidence that events or changes in circumstances have made recovery of the asset's carrying value unlikely. An impairment loss would be recognized when the sum of the expected, undiscounted future net cash flows is less than the carrying amount of the asset. The amount of the impairment loss would be recognized as the excess of the asset's carrying value over the fair value.

Investments in Available-for-Sale Securities
The company classifies its existing marketable equity securities as available-for-sale. INet valuation rules are: All of the company's securities, i.e. short- and long-term investments, are classified as available-for sale and reported at book value, with unrealized gains and losses reported in assets.

Derivative Financial Instruments
The company operates on the domestic market and is not in the position to reduce its exposure to fluctuations in interest rates and foreign exchange rates by creating offsetting positions through the use of derivative financial instruments.

Note 3 Income Taxes
According to the domestic legislation, the company is paying 15% income taxes.

Note 4 Segment Information
INet operates predominantly in a single industry segment as distributor of information technology products and services. The company's reportable measure of segment profits is income from operations. The accounting policies of the segments are those described in the summary of significant accounting policies. Geographic area in which the company operates include mainly the domestic market but also has developed its business in Kosovo (Serbia and Montenegro).

Note 5 Common Stock
The Shareholders Equity of the company is stated at the accounting value. The equity of INet is 100% private.The reserves are founded through distribution of the profit according to the domestic regulations.

INDEPENDENT AUDIT'S REPORT FOR THE YEAR 2007

Prepared by Deloitte DOOEL Skopje, on February 28, 2008

1. General information

INet AD, Skopje (hereinafter the "Entity") was established on April 21, 1991 as a company for construction and trading under the name Toning C.O., Skopje. In the period 1993-1999 the Entity changed its name and form of organization, and on May 10, 1999 it was registered as a limited liability company under the name INTERNET DOO, Skopje. On August 1, 2000 the Entity changed its form of organization into a shareholding company under the name INTERNET AD, Skopje. On July 19, 2001, the Entity changed its name into INet AD, Skopje confirmed by Decision No. 02-8467/5 issued by the State Statistic Office of the Republic of Macedonia.

The Entity is an authorized distributor of the products of IBM, Lenovo, Red Hat, SAP and Xerox.

The Entity's core business is distribution and sales of network and computer equipment and software as well as IT management services.

As of December 31, 2007, the Entity had 13 employees (December 31, 2006: 14).

2. Basis of preparation and presentation of the financial statements

The Entity maintains its accounting records and prepares its legal financial statements in accordance with the Article 469 of the Trade Company Law ("Official Gazette of the Republic of Macedonia" no. 28/2004 and 84/2005) and the Rulebook for Chart of Accounts ("Official Gazette of RM" no. 94/04, 11/2005 and 116/05). Following this Rulebook, the accounting standards applied in the Republic of Macedonia are International Accounting Standards (IAS) as of 2003 published by the International Accounting Standards Board (IASB). An addition to the Rulebook relates to the adoption of the International Financial Reporting Standard (IFRS) 1, published on February 10, 2005, as well as IFRS 2, 3, 4, 5, 6, and 7, published on December 28, 2005.

The accompanying financial statements are presented in the format prescribed by the Ministry of Finance ("Official Gazette" 113/06), which in some respects differs from the presentation of certain Balances as required under IAS 1 "Presentation of Financial Statements". Certain reclassifications have been made to present the accompanying financial statements in the format prescribed by that standard.

The amendments to the IAS and to the newly-issued IFRS released after the adoption of the aforementioned Rulebooks, have not been published and officially enacted in Republic of Macedonia, and accordingly, they have not been applied in the preparation of the accompanying financial statements.

The management is assessing the impact of the changes to the IAS, the newly-issued IFRS and to the interpretations to the financial statements. Although the majority of these changes are not applicable to the Branch's operations, the Branch's management does not express an explicit and unreserved statement in the accompanying consolidated financial statements of compliance with IAS and IFRS, which have been applied in the periods presented in the accompanying financial statements.

In the preparation of these financial statements, the Entity has adhered to the accounting policies described below, which are in conformity with the accounting and tax regulations prevailing in the Republic of Macedonia.
These financial statements are the Entity's stand-alone financial statements and they do not include the assets, liabilities, financial performance, changes in equity and cash flows of its subsidiary - IKS International Courier Services DOO – Skopje.

The Entity's reporting currency is the Macedonian Denar (hereinafter "Denar"). All amounts in the financial statements and the related notes are reported in thousand of Denars, unless otherwise stated.

3. Summary of significant accounting policies

3.1 Standards effective in the current period
In the current year, the Entity has adopted IFRS 7 Financial Instruments: Disclosures which is effective for annual reporting periods beginning on or after January 1, 2007. The impact of the adoption of IFRS 7 has been to expand the disclosures provided in these financial statements regarding the Entity's financial instruments and management of capital. Hence, such adoption does not reflect any changes of the accounting policies of the Entity, which are consistent with those from previous year.

The Entity management, following the requirements of this standard, has made certain presentation improvements. However, the practical implementation of certain aspects of the previous accounting practice with a view to achieving complete relevant conceptual compliance with the disclosure requirements pursuant to IFRS 7 is still pending. Hence, certain additional information and analysis regarding the Entity's financial instrument and management of capital are not presented in the manner required by this standard.

3.2 Revenue Recognition
The Entity recognizes revenues from the sale on domestic and foreign markets. The Entity recognizes revenues from the sale of goods when control is transferred, i.e. goods are delivered to customers. Revenues are recorded on an accrual basis, i.e. when they arise. Sales are stated at invoiced value, net of discounts and VAT.

3.3 Foreign Currency Translation
Transactions denominated in foreign currencies have been translated into Denars at official rates set by the National Bank of the Republic of Macedonia at the dates of the transaction. Net foreign exchange gains or losses, resulting from foreign currency translation, are included in the statement of operations. Assets and liabilities denominated in foreign currencies are translated at the balance sheet date using official rates of exchange ruling on that date.

3.4 Borrowing Costs
All costs associated with short-term and long-term borrowings are recognized as an expense in the statement of income in the period when they are incurred.

3.5 Cash and Cash Equivalents
For the purpose of the cash flow statement, cash and cash equivalents comprise of local and foreign currency funds at bank and cash in hand.

3.6 Trade Receivables
Trade receivables are stated at their nominal values as reduced by appropriate allowances for estimated irrecoverable amounts. An allowance for impairment of receivables is established when there is objective evidence that the Entity will not be able to collect all amounts due according to original terms of the receivables.

3.7 Inventories
Inventories consist of trade goods, communication equipment and software.
Inventories are measured at the lower of cost and net realizable value. Cost consists of the invoice amount and import duties and taxes, transportation costs and other cost related to the purchase.
The Entity applies FIFO method in calculating the cost of inventories.

3.8 Investments in Securities
Investment in securities is long-term investments in securities in banks, where the Entity has no influence and does not exercise control.
These investments in available for sale securities are initially recognized at cost, including transaction costs.

3.9 Equipment
Equipment is carried at cost upon their acquisition and is revalued annually using the official revaluation coefficients based on the general manufactured goods price index in the Republic of Macedonia. Such coefficients

are applied to historical cost or later valuation, and to accumulated depreciation. Effects of the revaluation are credited to the revaluation reserve, forming part of the equity. The last revaluation performed dates back to the year 2004.

Depreciation is charged on a straight-line basis at prescribed rates to allocate the cost of equipment, over their estimated useful lives. The annual depreciation rates applied are following:

	2007	2006
Motor vehicles	25%	25%
Computers	25%	25%
Furniture and equipment	20%	20%
Tools and accessories	15%	10%

When depreciable assets are retired or otherwise disposed of, the related cost and accumulated depreciation is removed from the respective accounts. Any gains or losses on disposal are recognized in operating revenues or operating expenses, respectively.

3.10 Taxation

Current Income Tax

Current income tax is calculated in accordance with the provisions of the relevant legislation of the Republic of Macedonia, based on the profit or loss recognized in the income statement prepared pursuant to Macedonian accounting regulations.

The estimated tax on monthly profit is paid in advance, as determined by the tax authorities. Final tax on profit are payable at rate of 12% (2006: 15%), based on the annual profit shown in the statutory profit and loss account.

Value Added Tax

Each sale of trade goods on the domestic market is subject to the VAT pursuant to the Law on Value Added Tax

Deferred Income Tax

Deferred income tax is to be provided by using the balance sheet liability method, for temporary differences arising between the tax bases of assets and liabilities and their carrying values in the financial statements. The currently enacted tax rates at the balance sheet date are used to determine the deferred income tax. Deferred tax liabilities are recognized for all taxable temporary differences. Deferred tax assets are recognized for deductible temporary differences and the tax effects of income tax losses are carried forward, to the extent that it is probable that taxable profit will be available against which the deductible temporary difference and the tax loss carry forwards may be utilized. The Entity's management assesses that there are no temporary differences as a basis for deferred income tax in these financials statements.

3.11 Employees Benefits

In accordance with the regulatory requirements, the Entity is obligated to pay contributions on salaries to tax authorities. These obligations involve payment of taxes and contributions to the Fund for Pension and Disability Insurance of the Republic of Macedonia (Pension Fund) and depend on the salary range. The Entity does not have defined benefit plans.

The Entity is obligated to pay retirement benefits in an amount equal to two monthly salaries earned by the employee. The management believes that the present value of the future obligations to employees, with respect to retirement benefits, is not materially significant and hence, it has not recognized a provision for the aforementioned payments. The Entity has not recognized a provision for the termination indemnities as considered not material.

3.12 Financial Instruments and Risk Management

Financial instruments are initially measured at cost, when the Entity becomes party to the contractual arrangements. The subsequent measurement of financial instruments is dealt with in the individual policy statements associated with the relevant item.

Financial instruments are classified as assets, liabilities or equity in accordance with the substance of the related contractual arrangement. Gains and losses relating to financial instruments are reported as income or expense, respectively. Financial instruments are offset when the Entity has a legally enforceable right to offset and intends to settle either on a net basis or to realize the asset and settle the liability simultaneously.
The Entity's risk management approach is focused on unpredictability of the financial market and seeks to minimize potential adverse effects. Risk management is carried out under the policies approved by the management.

3.13 Related Party Transactions

Related parties are those where one of the parties is controlled by the other or has significant influence in making financial and operating decisions of the other party.

3.14 Investments in Subsidiaries

The investment in subsidiaries is recognized at cost less any impairment.

4. Sales

In thousands of Denars
For the year ended December 31,

	2007	**2006**
Income from sales on domestic market	79.962	71.378
Income from sales on foreign market	68.706	19.792
	1.48.668	91.170

5. Other income

In thousands of Denars
For the year ended December 31,

	2007	**2006**
Write-off the payables	171	585
Credit notes	2.157	3.068
Capital gain from sale of vehicles	327	-
Other income	77	171
	2.732	3.824

The credit notes of Denar 2,157 thousand (2006: Denar 3,068 thousand) relate entirely to the credit notes received from Lenovo Singapure Pte Ltd, Singapure and IBM, Austria.

6. Staff costs

In thousands of Denars
For the year ended December 31,

	2007	**2006**
Gross Salaries	4.163	3.654
Per diems	438	843
Employees' allowances	1.159	1.288
	5.760	5.785

7. Other operating income

	In thousands of Denars For the year ended December 31,	
	2007	2006
Materials and consumables	215	172
Energy	553	441
Write-off of bad debts and doubtful trade receivables	291	143
Write-off of investments in securities	930	-
Transportation services	1.270	1.312
Maintenance	4.394	737
Fairs	-	117
Rent	747	748
Intellectual and consulting services	1.163	1.114
Entertainment	1.540	1.843
Insurance premiums	727	180
Taxes and contribution non-depending on income	154	125
Bank charges	1.076	940
Temporary engaged employees	3.919	3.297
Carrying amount of equipment and intangible assets written off	38	95
Other expenses	2.453	649
	19.470	11.913

8. Income tax

The tax charge for the year can be reconciled to the profit per the Income Statement as follows:

	In thousands of Denars	
	2007	2006
Profit before tax	4.181	408
Reconciliation of non-deductible income and expenses before tax purposes	3.474	1.995
tax relief on investment in fixed assets	-	(574)
Tax base after reconciliation	7.655	1.829
Income tax at income tax rate of 12% (2006:15%)	919	274

9. Cash and cash equivalents

	In thousands of Denars December 31,	December 31,
	2007	2006
Cash at banks in Denars	1.972	1.760
Cash at banks in foreign currency	3.809	1.881
Cash in hand	91	186
	5.872	3.827

10. Trade receivables

	In thousands of Denars December 31, 2007	December 31, 2006
Domestic trade receivables	10.017	14.534
Foreign trade receivables	1.632	1.217
	11.649	15.751

11. Inventories

	In thousands of Denars December 31, 2007	December 31, 2006
Trade goods on stock	10.805	7.505
Trade goods on reparing	95	54
	10.900	7.559

12. Other receivables

	In thousands of Denars December 31, 2007	December 31, 2006
Advances to suppliers	3	5
Receivable for overpaid VAT	669	271
Receivable for overpaid income tax	-	457
Receivables from employees	4	126
Prepayments	74	-
	750	859

13. Investment in subsidiaries

	In thousands of Denars December 31, 2007	December 31, 2006
IKS - International courier services DOO - Skopje	245	-
Aptiva Ltd - Pristina, Kosovo	31	-
	276	-

In August 2007, the Entity took a decision with Societe Anonyme SA - Athens, Greece to establish a company under the name IKS - International Courier Services based in Skopje. The Entity’s share in this subsidiary is 80%.

In November 2007, the Entity together with four other affiliates, took a decision to set up a company under the name Aptiva Ltd. based in Pristina, Kosovo. The Entity’s share in this subsidiary is 20%.

14 Equipment and intangible assets

Movements of equipment and intangible assets during 2007 are as follows:

	Equipment	Motor Vehicles	Total	Intangible Assets
Cost				
Balance, December 31, 2006	8.909	3.599	12.508	38
Additions	2.395	2.997	5.392	-
Disposals	(206)	(2.466)	(2.672)	-38
Balance, December 31, 2007	11.098	4.130	15.228	
Accumulated depreciation				
Balance, December 31, 2006	6.231	1.088	7.319	-
Charge for the year	993	839	1.832	-
Disposals	(206)	(1.130)	(1.336)	-
Balance, December 31, 2007	7.018	797	7.815	-
Net carrying amount at December 31, 2007	4.080	3.333	7.413	-
Net carrying amount at December 31, 2006	2.678	2.511	5.189	38

As of December 31, 2007, the motor vehicles with net carrying amount of Denar 3,333 thousand (December 31, 2006: Denar 2,412 thousand) were mortgaged as secured loans granted by TTK Banka AD, Skopje (Note 18).

15. Trade payables

	In thousands of Denars December 31, 2007	December 31, 2006
Domestic trade payables	5.843	2.636
Foreign trade payables	14.404	14.894
	20.247	17.530

16. Short-term loans

	In thousands of Denars December 31, 2007	December 31, 2006
Razvojna Fondacija Crimson, Skopje	-	5.574
Razvojna Fondacija Crimson, Skopje	2.500	-
	2.500	5.574

As of December 31, 2007, the short-term loan in the amount of Denar 2,500 thousand refers to the remaining part of the short-term loan granted in original amount of Denar 5,000 thousand by Razvojna Fondacija Crimson, Skopje approved on August 21, 2007 via Tutunska Banka AD – Skopje, with an interest rate of 9% p.a., payable in 4 installments of Denar 1,250 thousand each.

As of December 31, 2006, the short-term loan in the amount of Denar 5,574 thousand refers to the short-term loan received by Razvojna Fondacija Crimson, Skopje approved on October 31, 2006 via Tutunska banka AD - Skopje, with an interest rate of 10.5% p.a., payable in monthly instalments. The last instalment matured and was fully paid as of August 17, 2007.

17. Other current liabilities

	In thousands of Denars December 31, 2007	December 31, 2006
Advances received	154	290
Liabilities for income tax	462	
Liabilities for net salaries and contributions	329	330
Other liabilities to employees	52	209
Other liabilities	69	
	1.066	829

18. Long-term loans

	In thousands of Denars December 31, 2007	December 31, 2006
TTK Banka AD, Skopje - loan for purchasing a motor vehicle with an interest rate of 9.9% p.a. and 48 equal monthly installments out of which the last one will have matured as of November 11,2009	311	451
TTK Banka AD, Skopje - loan for purchasing a motor vehicle with an interest rate of 9.9% p.a. and 48 equal monthly installments out of which the last one will have matured as of January 4, 2010	998	1.406
Long-term loans in Denars	1.309	1.857
Current portion of long-term loans	613	531
	696	1326

The motor vehicles are pledged as loans security.

19. Equity

The share capital of the Entity as of December 31, 2007 consists of 13,844 authorized, issued and fully paid common shares with a nominal value of Euro 5 each.

Holders of common shares are entitled to the right of vote at a Shareholders' Assembly and qualify for dividend.

The structure of the shareholder's capital as of December 31, 2007, according to the Central Securities Depositary, is as follows:

	In Thousands of Denars	In EUR	%
Shareholders' capital			
Toni Petreski	2.539	41.530	80%
Aleksandar Naumovski	1.693	27.690	20%
	4.232	69.220	100%

Statutory Reserves
The Entity maintains obligatory reserves, as a common fund, by allocation of 15% from the net profit for the year. The allocation is required until the balance of the reserve reaches 1/5 of the Entity's share capital. Up to this minimum, the obligatory reserve can be used only for covering losses. Any excess over this minimum can be used for dividend distribution, if the founders issue such decision.

20. Financial instruments and risk management

Capital Risk Management
The Entity manages its capital to ensure that the Entity will be able to continue as a going concern while maximizing the return to stakeholders through the optimization of the debt and equity balance. he capital structure of the Entity consists of debt, which includes the borrowings disclosed in notes 16 and 18, cash and cash equivalents and equity attributable to equity holders, comprising shareholders' capital, reserves and accumulated loss.
The Management reviews the capital structure on a monthly basis. As a general rule, purchasing of non-current assets are financed by long-term borrowings secured through banks and they are most frequently guaranteed by a pledge for the equipment purchases.

The gearing ratio at the year end was as follows:

In thousands of Denars

	2007	2006
Borrowings (short-term and long-term)	3.809	7.431
Cash and cash equivalents	5.872	3.827
Net debt	(2063)	3.604
Total equity	11.750	8.488
Net debt to equity ratio	(18%)	42%

The Entity's principal financial instruments are trade and other receivables, available-for-sale financial assets and cash and cash equivalents which arise directly from its operations and trade and other payables and borrowings which main purpose are to raise finance to the Entity's operations. In the normal course of operations, the Entity is exposed to the following risks:

Interest rate risk
The interest rate risk based on which the Entity's liabilities arising from borrowings might be changed as a result of interest rate changes in the financial market.

Foreign currency risk
The Entity enters into transactions denominated in foreign currencies related to the purchase and sale of trade goods and long-term borrowings. The Entity does not use any special financial instruments to hedge against these risks since such instruments are not in common use in the Republic of Macedonia. Therefore the Entity is potentially exposed to market risk related to possible foreign currency fluctuations which is adjusted to a certain extent through offsetting debit and credit balance of each foreign currency.
The Entity undertakes certain transactions denominated in foreign currency. Exchange rate exposures are measured within approved policy parameters. The carrying amount of the Entity's foreign currency denominated monetary assets and monetary liabilities at the reporting date are as follows:

	Liabilities In Thousands of Denars		Assets In Thousands of Denars	
	2007	2006	2007	2006
EUR	5.114	3.197	4.306	2.084
USD	13.099	19.308	1.135	1.014

The following table details the Entity's sensitivity analysis to a 10% increase and decrease in the Currency Unit – Denar ("CU") against the relevant foreign currency. 10% us the sensitivity rate used when reporting foreign currency risk internally to key management personnel and represents management's assessment of the reasonably possible change in foreign exchange rates. The sensitivity analysis includes only outstanding foreign currency denominated monetary items and adjust their translation at the period end for a 10% change in foreign currency rates. A positive number below indicates an increase in profit and equity where the CU strengthens 10% against the relevant currency. For a 10% weakening of the CU against the relevant currency, there would be an equal and opposite impact on the profit and equity.

	Increase of 10% in CU In Thousands of Denars		**Decrease of 10% in CU In Thousands of Denars**	
	2007	**2006**	**2007**	**2006**
Net exposure in EUR	(81)	(112)	81	112
Net exposure in USD	(1.197)	(1.829)	1.197	1.829
Profit and loss and equity	(1.278)	(1.941)	1.278	1.941

The Entity's sensitivity to foreign currency has decreased during the current period mainly due to decrease of borrowings denominated in USD.

Credit Risk

The Entity's credit risk exposure is primarily attributable to its trade receivables and payables. Significant credit risk exposure exists in respect of its large counterparties and it is managed through Entity's credit policies and procedures.

Liquidity risk

The ultimate responsibility for liquidity risk management rest with the management of the Entity, which built liquidity risk management framework for the management of the Entity's short and medium funding and liquidity management requirements. The Entity manages liquidity risk by maintaining adequate cash reserves to pay third party creditors. At any time, the Entity can draw additional borrowings from banks. Majority of the maturity for its trade and other payables lies within 1-3 months and the borrowings mature in accordance with the agreed terms with banks.

Tax Risk

The Macedonian tax legislation is subject to varying interpretations and changes occur frequently. The interpretation of tax legislation by tax authorities as applied to the transactions and activity of the Entity may not coincide with that of the management. As a result, transactions may be challenged by tax authorities and the Entity may be assessed additional taxes, penalties and interest, which can be significant. The periods remain open to review by the tax and customs authorities with respect to tax liabilities for five years.

Fair value of financial instruments

The management considers that the carrying amounts of financial instruments in the financial statements approximate their fair values.

21. Related party transactions

In the course of 2007 and 2006 the Entity did not enter into any transactions nor has it any receivables and liabilities balances with related parties as of December 31, 2007 and 2006.

22. Post balance sheet events

Effective from January 1, 2008, in accordance with the changes of the local tax regulation, new lower tax rates were introduced in respect of income tax and personal income tax which decreased from 12% to 10%.

23. Exchange rates

Official exchange rates for major currencies used in the translation of the balance sheet items denominated in foreign currencies, as of December 31, 2007 and 2006, were as follows:

	December 31, 2007	December 31, 2006
EUR	41,6564	46,4496
USD	61,2061	61,1741