

ANNUAL BUSINESS REPORT FOR 2013



 *Telekom Srbija* **2013.**

**ANNUAL BUSINESS REPORT
TELEKOM SRBIJA A.D.
FOR 2013**

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SUMMARY REPORT



TELECOMMUNICATIONS COMPANY "TELEKOM SRBIJA" A.D., BEOGRAD

On 23 May 1997, the Public Enterprise of PTT Traffic "Srbija", Beograd (PE PTT or PE of PTT Traffic "Srbija") established the Telecommunications Company "Telekom Srbija" a.d., Beograd (hereinafter: Telekom Srbija or the Company or the Parent Company) when it

assigned to the Company all telecommunications assets, including real estate and some other assets and liabilities. The Company was registered on 29 May 1997 as a joint stock company, incorporated for an indefinite period of time.

In accordance with the Law on Business Companies (Official Gazette of RS, no. 36 of 27 May 2011 and no. 99 of 27 December 2011), the Company's General Meeting adopted the Articles of Association in 2012, defining the

following management bodies in the Company: the General Meeting, the Supervisory Board and the Executive Board.

The Company's core activity is the provision of telecommunications services, the most important being the services of local and international telephone traffic, fixed telephone services, traffic transit, data transfer, lease of lines, services in the entire network area, add-on services in the field of mobile telephony, fixed services, the Internet and multimedia services. The Company's predominant activity, according to the applicable activity classification, is the cable telecommunications activity.

The Company also provides services in the area of lease, construction, management and protection of telecommunications infrastructure, it issues telephone directories, provides operator-assisted call services and e-directory services in the field of fixed telephone services.

The Company has a mobile telephony licence (GSM/GSM1800 and UMTS/IMT-2000). In 2007, the Company renewed the fixed telephony licence. Since 2009, the Company has been in possession of a fixed wireless access licence (CDMA).

In keeping with the Law on Electronic Communications (Official Gazette of RS no. 44, of 30 June 2010 and 60/2013) the Republic Agency for Electronic Communications (RATEL or the Agency) has defined nine markets that are subject to previous regulation.

Various obligations have been imposed upon the operator depending on the market where it was declared an SMP operator. Among others, the following obligations are prescribed for an SMP operator: announcing certain information in a standard offer form, non-discriminatory actions, enabling access and using network elements and associated facilities, price control, application of cost accounting,

prohibition of charging excessive fees, tariff control, etc.

Telekom Srbija was declared an SMP operator in 2011 in all markets, save for the retail market of media content distribution.

Telekom Srbija is a joint stock company whose registered, authorised, issued and paid-in capital consists of 1,000,000,000 ordinary shares.

As at 31 December 2013, Telekom Srbija has a share in the capital of the following subsidiaries:

- *"Telekomunikacije Republike Srpske" a.d. Banja Luka, Republika Srpska, i.e. Mtel a.d. Banja Luka (65% of share capital);*
- *Društvo za telekomunikacije d.o.o. Podgorica (telecommunications company), "mtel" DOO, Podgorica, Crna Gora (51% of capital);*
- *Privredno društvo za održavanje i obezbeđivanje objekata, imovine i druge usluge „Telus“ akcionarsko društvo, (Company for providing maintenance and security of facilities, property and other services) Beograd, Republika Srbija (100% of share capital);*
- *Društvo za telekomunikacije „FiberNet“ DOO (Telecommunications Company), Podgorica, Crna Gora (100% of capital);*
- *TS:NET B.V., Amsterdam, the Netherlands (100% of capital); and*
- *Društvo za telekomunikacije „HD-WIN“ d.o.o. (Telecommunications Company), Beograd, Republika Srbija (51% of capital).*

SUMMARY REPORT

INTRODUCTORY NOTE BY THE DIRECTOR GENERAL

Dear Sirs/Madams,

The Company's business operations in 2013 were marked by the trends present in our market for a number of years. As a consequence of heavy legacy issues, the whole public sector and economy were faced with numerous challenges, and the resulting position of citizens could not be satisfactory either.

Nevertheless, in 2013, we remained firmly committed to fulfilling our business goals so as to be even better prepared for a fierce market competition that was taking place and was becoming increasingly stronger. That is why we can be satisfied with the achieved results.

We achieved considerable growth of net profits, both on the Company level and on the level of the Parent Company and its subsidiaries. It was primarily influenced by stabilisation of the foreign exchange rate in the Republic of Serbia and repayment of significant portion of loans.

We succeeded in reducing the level of operating expenses by applying control measures, both on the Company level and on the level of the Parent Company and its subsidiaries.

Operating revenues and EBITDA have, likewise, recorded a slight decline on the Company level and on the level of the Parent Company and its subsidiaries.

The pressure by the competition and the regulator in all market segments were evident, and it was reflected both in the realized revenue and in the number of customers. Notwithstanding the circumstances, in 2013 we succeeded in arresting the progress of some negative trends from the past, primarily in mobile telephony.

Mobile telephony recorded a slight increase in the number of customers and significant change in their structure in favour of postpaid customers. Attractive service bundles offered to our customers and the quality of network and services made a hefty contribution to reversing the trend.

The number of customers and the traffic generated in fixed telephony are on a downward path, in keeping with the global trend. The number of our *broadband* and IPTV customers already has a stable growth, while our BOX bundle is getting stronger year over year, and it makes a strong distinction versus our competition.

Significant investments in 2013 were targeted to maintenance and increasing the network quality in all segments. Our goal was to enable higher bitrates in data transfer and the quality of all other services, but also to introduce new services, in the domain of integrated ICT services, among others.

In 2013, we ensured financial stability and regularly settled all our liabilities towards creditors, we conducted a re-organisation for the purpose of achieving efficiency of business processes and bringing our services closer to our customers.

In 2013, the decision on payment of an interim dividend of RSD 7.6 billion was passed, which was paid out to our shareholders by this time.

We expect to be facing new challenges in the market and society in the following year as well. We can expect a strong pressure by the competition and the regulator in all segments, particularly in fixed telephony through the introduction of number portability option.

We will respond to such challenges by making further investments in our network and by introducing new services and service bundles, whereby we will facilitate our customers to use, in an affordable fashion, a wide portfolio of the services we offer.

It will require increased efforts and commitment, both on the part of the management and on the part of employees, achievement of strategic goals which is to be defined in a new Strategic Business Plan, together with innovation of services and technology, and maximum deployment of all resources: human, financial and technical and technological ones and additionally improved optimization of operating expenses.

Our intention is to retain the position of the regional leader in all spheres of business activities by making sound strategic decisions.

Next year, as all these years, Telekom Srbija will continue building its reputation as one of the leading socially responsible companies, that proactively acts in all spheres of cultural, social and sports life, through cooperation with and support to the community and individuals.

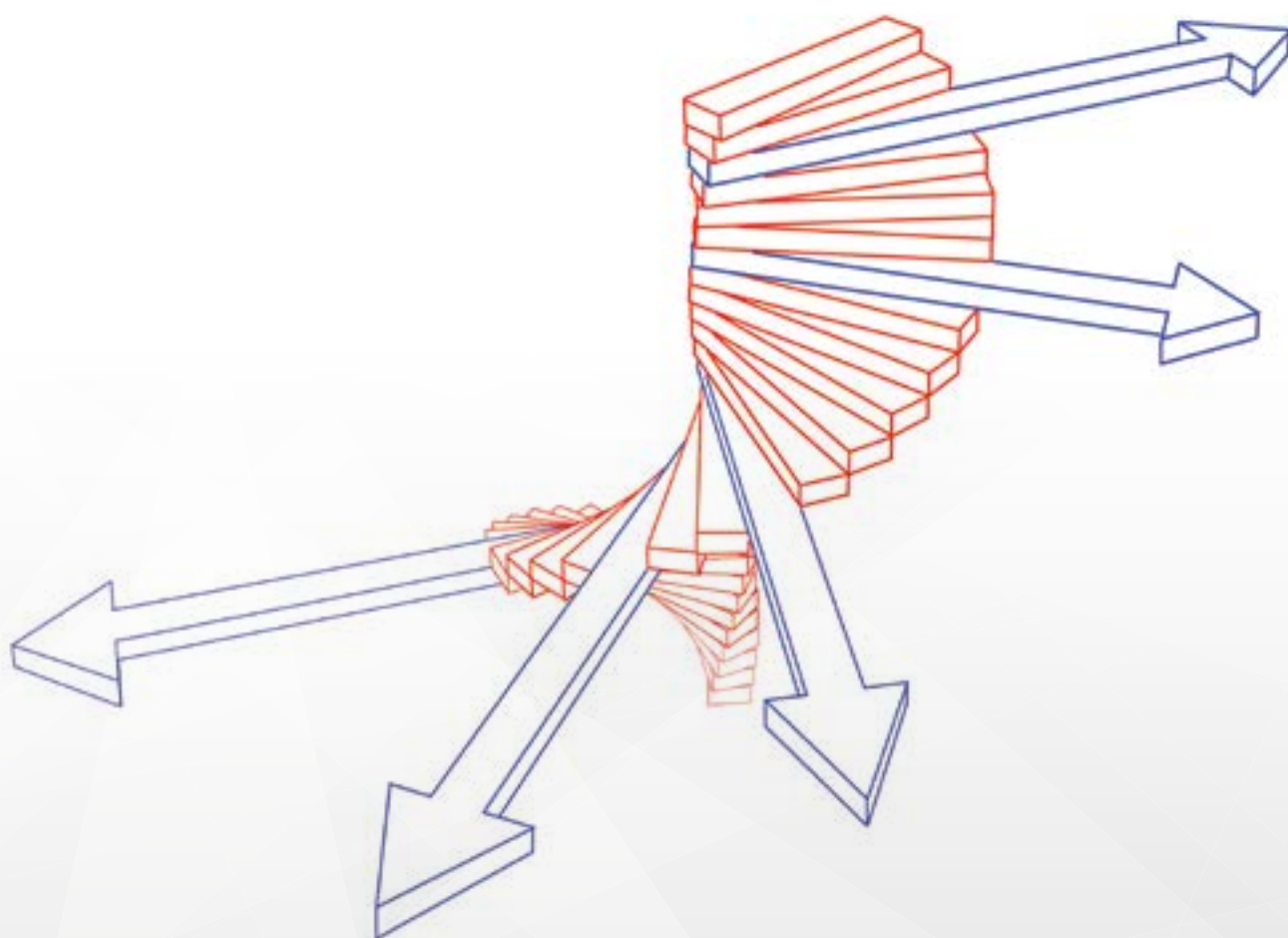
I would like to thank all our shareholders, business partners, employees and everybody else who recognize our ideas and support our vision that Telekom Srbija a.d. Beograd, as a national company, should be a modern one and keep up with all trends in the present communications market. I particularly thank our loyal customers who show us their trust and who are the reason why we exist so long and so successfully in the market.

I invite you to continue sharing our vision in the future.

Cordially yours,
Predrag Ćulibrk

Director General of Telekom Srbija a.d.
Beograd

DEVELOPMENT AND BUSINESS ENVIRONMENT



BACKGROUND

May 1997 - the Public Enterprise of PTT Traffic "Srbija" (hereinafter: PE PTT) founded, as single-member joint-stock company, Telecommunications Company Telekom Srbija (hereinafter: Telekom Srbija or the Company or the Parent Company).

June 1997 - Within the privatization of a part of the capital, 49% of shares were sold to STET INTERNATIONAL NETHERLANDS N.V., affiliation of the Italian Telecommunications Company Telecom Italia in the Netherlands (29% of shares) and to Greek Telecommunications Company HELLENIC TELECOMMUNICATIONS ORGANIZATION S.A. (OTE) (20% of shares).

February 2003 - An agreement was concluded whereunder PE PTT bought back the entire package of Telekom Srbija shares, owned by Telecom Italia, and thus acquired a total of 80% shares in Telekom Srbija, while the remaining 20% of shares stayed in the ownership of OTE.

September 2010 - Based on the Conclusion of the Serbian Government 05 number 023-6816 of 21 September 2010 and Decision of the Managing Board of PE PTT of 20 September 2010 on the free transfer of shares in Telekom Srbija to the Republic of Serbia, the PE PTT and the Serbian Government concluded the Agreement on the Free Transfer of Telekom Srbija's Shares – Gift on 24 September 2010. By virtue of this agreement, the Republic of Serbia became the majority owner of Telekom Srbija and acquired the ownership right to 80% of the shares in Telekom Srbija, while 20% of the shares remained in the ownership of OTE.

December 2011 –On 16 December 2011, the General Meeting of Telekom Srbija passed the Decision on the Acquisition of Own Shares, previously owned by OTE, as the Company's minority shareholder, whereunder the General Meeting approved the conclusion of the Share Sale Agreement between Telekom Srbija

and Hellenic Telecommunications Organization S.A., which was eventually signed on 30 December 2011.

January 2012 - On 25 January 2012, Telekom Srbija paid in full the funds against the stake of the minority shareholder OTE in the capital of Telekom Srbija. Since that date, Telekom Srbija has become the owner of 20% of shares.

May 2012 - Under the Decision of the Serbian Government on the Free Transfer of Shares to the Citizens – Right Holders and Employees and Former Employees of Telecommunications Company Telekom Srbija a.d. of 27 April 2012, and in accordance with the Law on the Right to Free Shares and a Monetary Compensation Exercised by Citizens in the Privatization Procedure (the Official Gazette of RS, No. 123/07 and 30/10), the procedure for and the manner of the transfer of free shares of Telekom Srbija to the citizens as the holders of such right and employees and former employees of Telekom Srbija, including the employees and former employees of PE PTT and their legal predecessors was defined, and based on such procedure the distribution of free shares was carried out. After the distribution of free shares, the structure of Telekom Srbija's equity changed, so that the stake of the Republic of Serbia was 58.11%, the stake of Telekom Srbija was 20%, the Serbian citizens acquired 14.95% and the employees and former employees acquired 6.94% of shares in Telekom Srbija.

DEVELOPMENT AND BUSINESS ENVIRONMENT

MARKET

Macroeconomic data

During Q4 of 2012 and early 2013, macroeconomic indicators showed signs of improvement: economic activity was slowly recovering, inflation came to an abrupt halt, while the foreign trade deficit was decreasing.

The information about economic trends in 2013 has been evaluated based on the available and published data. The real GDP growth, in terms of the prices from the last year, in Q4 of 2013, versus the same period last year, accounted for 2.7%. GDP expressed in current prices in 2013 amounts to RSD 3,761.3 billion.

Consumer prices in December 2013, compared to the same month 2012, increased by 2.2%, while the average annual growth equalled 7.8%.

Industrial production in the Republic of Serbia in December 2013 was 0.5% higher compared to December 2012, or 9.5% higher compared to the 2012 average. Industrial production in the January – December 2013 period, versus the same period 2012, was 5.5% higher.

The following sector-specific trends were recorded in December 2013, compared to the same month in 2012:

- Sector of power-supply, gas, steam and air-conditioning - 5.9% growth,
- Mining sector – 5.7% growth, and
- Processing industry sector - 1.9% fall.

The strongest influence upon the growth of industrial production in 2013, versus 2012, can be attributed to: production of motor vehicles and trailers, production of oil derivatives, electric power production and the production of chemicals and chemical products.

Total foreign trade commodity exchange of the Republic of Serbia for the January-December 2013 period amounts to:

- USD 35,157.4 million – 16.6% growth compared to the same period last year;
- EUR 26,462.1 million – 12.8% growth compared to the same period last year.

The deficit amounts to USD 5,928.6 million, which accounts for 23% decrease compared to the same period last year.

The export/import coverage index equals 71.1% and it is higher than that in the same period last year, when it equalled 59.3%.

Inflationary pressures in 2013 were rather low, particularly in the second half of the year, when the average monthly inflation rate equalled –0.1%. Along with a low aggregate demand, a good agricultural season and, consequently, lower food production costs were a significant disinflationary element, while the largest pressure upon inflation was made by regulated prices – almost the entire growth of prices in 2013 (2.2%) owes to the growth of regulated prices (contribution 2,1 p.p.).¹

The average salary without taxes and contributions disbursed in 2013 in the Republic of Serbia, compared to 2012, was 6.2% higher in nominal, or 1.5% lower in real values. The average net salary of employees in the Republic of Serbia in 2013 was RSD 43.932.²

According to the results of the Survey of Work Force from October 2013, the unemployment rate, compared to data from April, dropped by 4.0 p.p., to 20.1%. In the same period, the employment rate increased by 2.8 p.p., and the activity rate by 1.1 p.p.

1. <http://www.nbs.rs/internet/cirilica/index.html>

2. <http://www.cekos.rs/prose%C4%8Dne-bruto-zarade-plate-decembar-2013-godine>

According to the information provided by the National Employment Service, the number of unemployed, following two declining quarters, has seen an increase in Q4 by 10,174, totalling 769,546 persons.

In early 2013, the reference interest rate equalled 11.5% and was reduced to 9.5% by the end of the year.

The balance-of-payments deficit was reduced to 5.0% of GDP, primarily owing to sharp rise of export in automotive and oil industries.

Regulations

In accordance with the Law on Electronic Communications (Official Gazette of RS no. 44/10) and the licences issued by the Republic Agency for Electronic Communications, as the competent regulatory body, (hereinafter: RATEL), Telekomunikations Company "Telekom Srbija" a.d., Beograd performs the activity of electronic communications, which includes: construction and installation, maintenance, using and granting the use of public communications networks and associated facilities, as well as the provision of publicly available electronic services.

In keeping with the Law on Telecommunications, the Rules on the number and period for which the licence for public mobile telecommunications networks and services is issued, and minimum requirements and minimum amount of one-off fee for licence issuance (Official Gazette of RS no. 29/06 and 77/06), in a procedure of replacing the existing GSM/GSM1800 licence, RATEL issued to the Company, on 28 July 2006, the Licence for public mobile telecommunications network and services of public mobile telecommunications network, in keeping with GSM/GSM 1800 and UMTS/IMT-2000 standards, which was issued for a 10-year period. After the expiry of the said period, the Licence validity is to be extended

to further 10-year period, without a demand by Telekom Srbija, provided that the Licence requirements have been met.

On 13 April 2007, in accordance with the Law on Telecommunications, the Company was granted by RATEL, in a replacement procedure, a Licence for construction, possession and operation of public fixed telecommunications network and provision of services of public fixed telecommunications network, issued for the period until 9th of June 2017. After the expiry of the said deadline, Telekom Srbija may file a request for extending the Licence validity, no later than six months prior to the expiry of this Licence.

On 16 June 2009, the Company was granted the Licence for public fixed wireless telecommunications network (FWA) and for voice services, data packet transfer and simultaneous voice and data transfer (CDMA licence). The licence was issued for a period of 10 years, where the provision of commercial services was to start within six months from the Licence effective date.

Among the activities related to regulatory framework, bearing the implications upon the Company's operations in 2013, we emphasise the following:

- The Company conducted administrative and technical preparations for the process of number portability in fixed network, in accordance with the obligation provided for in the Rules on Number Portability in Public Telephone Networks at a Fixed Location, the commencement of which is projected for 1 April 2014.
- Regulatory Report for 2012 was submitted to RATEL in conformity with the new model (current cost accounting – CCA), as one of the bases for prescribing the prices of regulated services by RATEL.

DEVELOPMENT AND BUSINESS ENVIRONMENT

Telecommunications market

Telecommunications market in the Republic of Serbia has been regulated and gradually liberalized per operating segment since 2006. According to preliminary data of the Republic Electronic Communications Agency, the overall share of telecommunications in the Serbian GDP in 2013 remains on the stable level of almost 5%, with total revenue of EUR 1.6 billion and investments that record 13.4% growth, in the amount of EUR 262 million.

The largest share in the overall revenues belongs to mobile telephony with 56.3% and fixed with 20.9%, followed by the Internet services with 11.9% share and distribution of media content with 7.53%.

The development of IT sector is followed by legal and regulatory activities and liberalization of regulatory regime, including the adoption of the Strategy of Development of Information Society in Serbia by 2020, and the introduction of e-governance program in a number of state institutions.

The fixed telephony market may be said to have entered the liberalisation phase, which will be finalized by the introduction of number portability as of 1 April 2014. As is the case with other markets of fixed telephony, the trend of migration to digital telephony is evident. Likewise, there is an apparently decreased traffic volume through fixed networks due to increasingly dominant share of mobile telephony. However, the importance of this market is still high, as evidenced by the fact that it is only now that some companies are emerging in this segment.

In addition to Telekom Srbija, the companies that have operated in the market of fixed telephony since 2009 are Orion telekom d.o.o., Beograd, formerly known as Media Works, then Telenor d.o.o., Beograd that was granted the licence for public fixed telecommunications

network and services in 2010. In 2012, the licences were also granted to Serbia Broadband – Srpske kablovske mreže d.o.o., Beograd, IKOM d.o.o. Beograd and Invest Inženjering d.o.o., Novi Sad, and in 2013 the companies Beogrid d.o.o., Beograd, Knight Development Support, Novi Sad and JET TV, Šabac entered the fixed telephony market in Serbia whereby the number of operators possessing the fixed telephony licence was increased to nine.

According to RATEL's preliminary data for 2013, there were around three million fixed customers in Serbia. Telekom Srbija's operations in fixed telephony segment remains dominant, both in financial and in technical terms.

In mobile telephony market there are still three operators in place: Telekom Srbija a.d., Telenor d.o.o. Beograd and Vip mobile d.o.o. Beograd. All three operators possess licences for public mobile telecommunications network and the services of public mobile telecommunications network in conformity with GSM/GSM1800 and UMTS/IMT-2000 standards issued by Ratel. The licences have been issued for the territory of the Republic of Serbia, for a 10-year period, whereafter the licence validity will be extended for a next 10-year period, for which the licence holder shall not be required to file a request, provided that all requirements from the licence have been fulfilled.

Several segments of mobile telephony can be considered stable, with a slight increase in the number of customers, primarily those using postpaid services.

The Republic Agency for Electronic Communications announced that the migration of numbers from one to another network in 2013 was increased by 5% in 2013 compared to the previous year.

The Internet market in the Republic of Serbia in 2013 continued the rising trend from the previous years. ADSL is still the most common mode of the Internet access. The Internet

access can be also established by means of a cable modem, directly, via Ethernet, by fibre optic cable, wirelessly in bandwidths of 2.4 GHz and 5.8 GHz, which are in free usage mode, in fewer cases by using bandwidths 3.4-3.6 GHz and via UMTS (3G) network of mobile operators.

According to the data of the Republic Statistics Office, in 2013, 59.9% households in Serbia had a computer, which accounts for 4.7% increase, while 55.8% households had the Internet connectivity, i.e. 8.3% increase compared to the previous year. More than 2.6 million persons used computers every day, and more than 2.4 million persons used the Internet on a daily basis. A part of the research conducted by the Republic Statistics Office, related to companies, shows that 100% use computers in their business, 99.6% have the Internet access, while 87.6% use the electronic services of public administration.

ADSL retail segment will remain a significant growth driver in the forthcoming period.

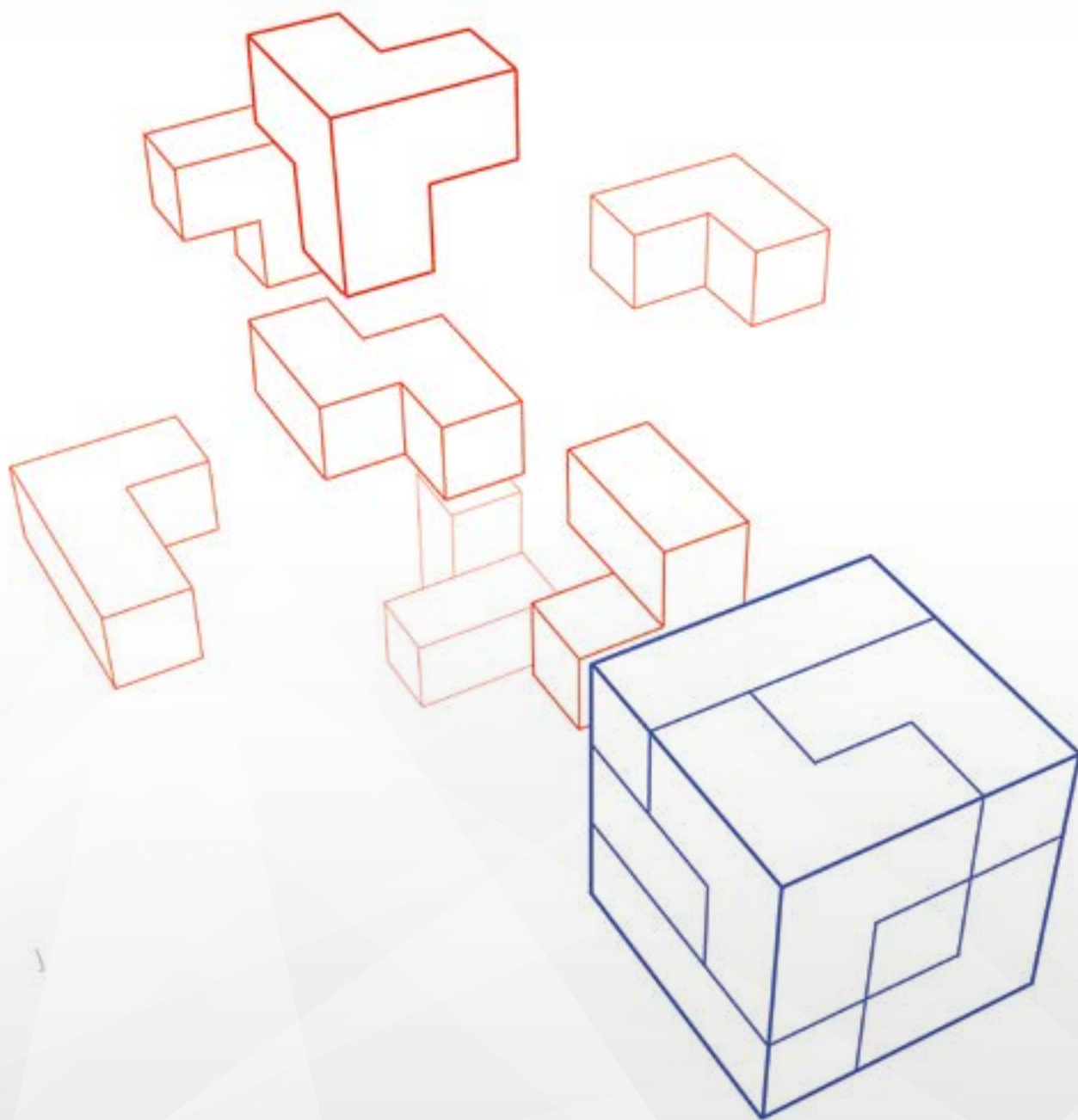
The market of media content distribution in the Republic of Serbia was not significantly changed in 2013. The operators provided their services through the following public telecommunications networks:

- Cable distribution network (coaxial, hybrid and optical) – KDS, which include analogue and digital cable distribution system;
- Public fixed telephone network– IPTV;
- Satellite distribution network (*Direct to Home*) – DTH.
- In 2013, 36 operators pursued their business activities in Serbia, predominantly OpenIPTV and PTT KDS. The digital platform is undeveloped, and consequently Pay packages as well. DTH platform Polaris Media is used, which is also the

main mode of distribution of Arenasport channel, owned by our subsidiary HD-WIN, and the market coverage of this subsidiary is around 50%.

- In order to enhance the service and its quality, customer retention, defending the market position, and strengthening the Company's image as the operator that provides all types of services, Telekom Srbija constantly enriches its Box packages, or bundled services, by incorporating several services in a unified offer.

CORPORATE MANAGEMENT



CORPORATE MANAGEMENT

Corporate management is a system for the management and control of business companies. Such management approach makes it possible for Telekom Srbija to implement better mechanisms of organization and control and assign competences in an efficient manner. This approach also enables Telekom Srbija to gain the trust of potential investors. The distinction between the ownership right and the management of Telekom Srbija, responsibility towards the shareholders, taking care of the shareholders' interests, transparency and mandatory information requirements represent the current principles which provide for better results.

A good corporate management is the practice that also contributes to a sustainable economic growth by improving the business result of the Company, the company growth and profitability. As a business company that is engaged in one of the core infrastructure activities in the society, Telekom Srbija thus provides an incentive to the numerous business partners and to the society, as a whole.

Corporate Bodies and Corporate Management System

In order to organize the management of the Company and respond to the business challenges in the best possible way, Telekom Srbija, as a responsible company, is organized as a two-tier system of management. The bodies of Telekom Srbija are:

- General Meeting
- Supervisory Board
- Executive Board

The Company represents a single business system structured by the functional, territorial and market-based principle, which accomplish its operating goals through the operating units headed by the executive directors.

The scheme on the next page shows the organizational structure of Telekom Srbija.

GENERAL MEETING

The General Meeting is a corporate body of the Company where the shareholders may exercise their ownership rights. The General Meeting is composed of all shareholders of the Company. In 2013, two sessions of the General Meeting were held: 45th regular session of the General Meeting held on 27 June 2013 and 46th extraordinary session of the General Meeting held on 18 December 2013.

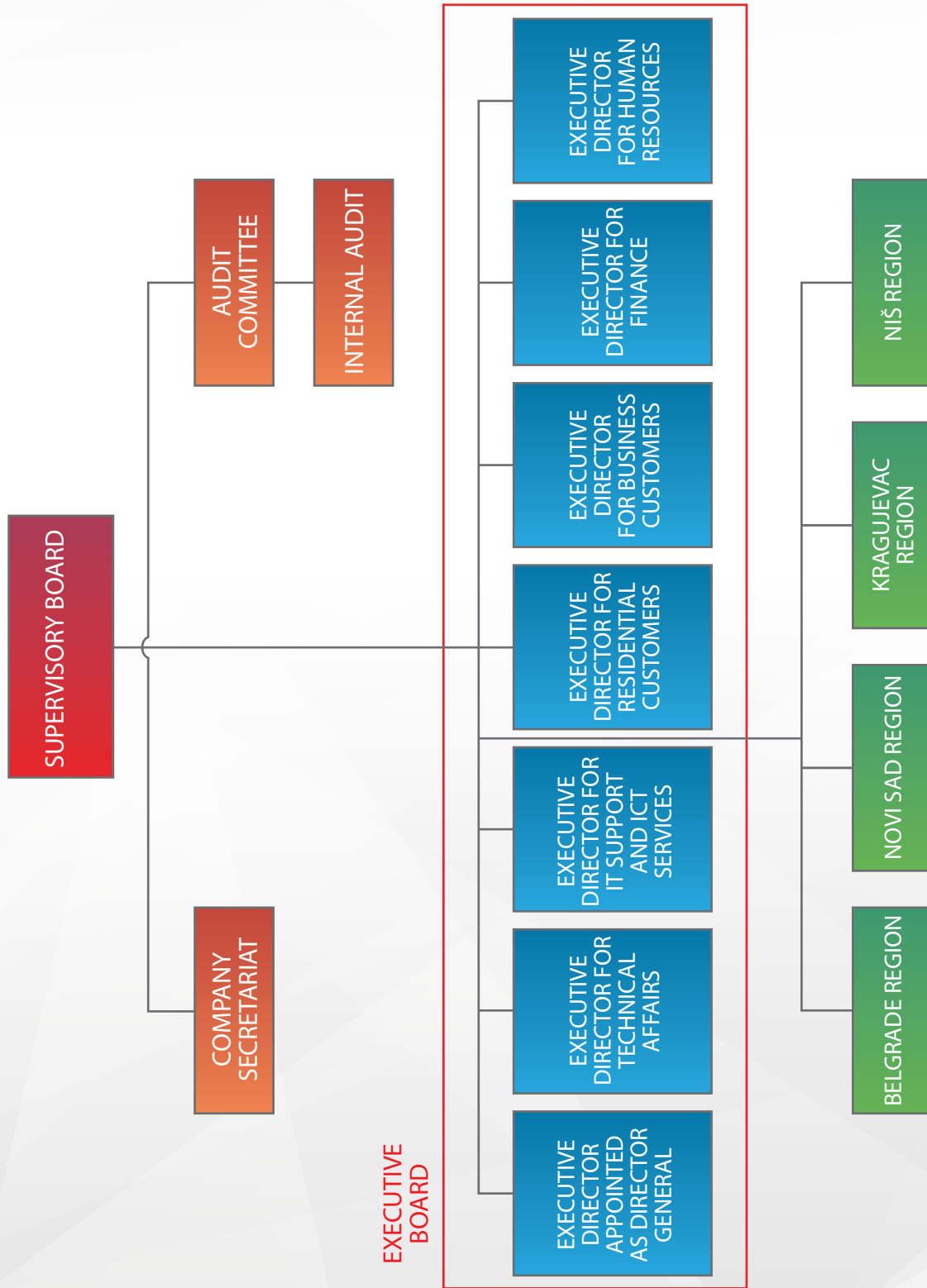
SHAREHOLDERS' RIGHTS

The Company guarantees for the ownership and non-ownership rights of the shareholders as stipulated by the Law, the Memorandum of Incorporation, the Articles of Association and other Company by-laws.

The Company is guided by the principle of equal and fair treatment of shareholders and takes the measures to that end, including in particular:

- providing that the shares of the same class bear the same rights,
- timely and regular provision of relevant information about the Company (including the information available on the Company website),
- participating and voting at the General Meeting session,
- provision of the timely, true and full information about the issues of particular importance for the Company's operation concerning the significant corporate changes, particularly the amendments to the Articles of Association, decrease or increase in capital, major changes in the ownership structure, status-related changes and changes in the legal form and disposition of high-value assets,

CORPORATE MANAGEMENT



Telekom Srbija Organizational Structure

- ensuring the equal treatment of all shareholders (including the minority and foreign shareholders), especially the efficient legal protection of the rights of the minority shareholders against any abuses by the majority shareholders.

The Company prohibits and shall continue to combat any unauthorized trade in shares based on confidential (insider) information and any possible cases of abuse that may occur in connection with any transactions made.

SUPERVISORY BOARD

The Supervisory Board is a corporate body of the Company. The number of the members of the Supervisory Board is established by the Company Articles of Association observing the principle setting forth that the prescribed number should provide for a continuous operation with a team possessing the skills and expertise necessary for the operation of the Supervisory Board. The Supervisory Board consists of 7(seven) members of whom at least one member is an independent member in accordance with the applicable Law on Business Companies.

The Supervisory Board and the members thereof shall be conscientious and loyal to the Company and the shareholders and shall perform the tasks falling within the scope of their responsibility with due diligence and with the reasonable belief that their actions are in the Company's best interest.

The members of the Supervisory Board shall:

- base their decisions on a reasonable and competent judgement and all available information and opinions rendered by the relevant experts,
- observe the rules related to the conclusion of transactions that involve any personal interest and competition ban in any dealing and/or legal transaction which is entered into by the Company or which is subject to a decision of the Bodies,
- during and after the expiry of their terms of office, treat the data and material concerning the Company as confidential information no matter whether such information is confidential, in accordance with the Company's policy and internal by-laws governing confidential information.

The Supervisory Board members are elected by the General Meeting by a simple majority vote of the attending or represented members with a voting right and the shareholders that vote through the circulation of papers, in accordance with the Law and the Articles of Association.

The candidates for the Supervisory Board members are nominated by the Supervisory Board, the Appointment Commission, if any, or by the Company's shareholders who have the right to propose the agenda for the General Meeting session.

AUDIT COMMISSION OF THE SUPERVISORY BOARD

In order to increase the operating efficiency and in accordance with the Articles of Association of Telekom Srbija, on 13 December 2012, the Supervisory Board passed a decision on setting up the Audit Commission of the Supervisory Board of Telekom Srbija a.d. The Audit Commission is responsible for its work to the Supervisory Board of the Company and is obliged to submit the reports on the operations and activities taken by it, in compliance with the competences laid down by the applicable legal regulations, at least twice a year any time the Supervisory Board requests such reports to be submitted. The Audit Commission has 3 (three) members one of whom is the chairman of the Commission.

The Audit Commission oversees, but does not manage, the process of financial reporting. Its role is primarily to ensure that the procedures, actions and audits performed by the management and the external auditor provide for

CORPORATE MANAGEMENT

the identification and remedy of errors and irregularities, i.e. make it possible for them to prepare and issue the financial statements in a fair and adequate manner. Likewise, the Audit Commission supervises the performance of tasks related to the internal supervision of the Company and nominates the manager of the organizational unit in charge of internal supervision in the Company.

The Supervisory Board endeavoured to appoint to the Commission persons of adequate professional and personal characteristics and experts in relevant fields.

EXECUTIVE BOARD

The members of the Executive Board, including the Director General, are elected by the Supervisory Board. The members of the Executive Board are executive directors. The Executive Board has 7 (seven) members. The Executive Directors, i.e. the Executive Board manages the Company's activities within the respective scope of responsibilities set forth under the Law and the Company internal by-laws.

COMPANY SECRETARY

Telekom Srbija has the Company Secretary that is appointed by the Supervisory Board. The competences of the Company Secretary are governed by the Articles of Association of the Company and the relevant decisions of the Supervisory Board.

STATEMENT ON THE APPLICATION OF THE CODE OF CORPORATE MANAGEMENT

Telekom Srbija has been applying the Corporate Management Code adopted at the 1st session of the Supervisory Board of the Company on 26 June 2012 and published on the Company's website www.telekom.rs. The Company strives to develop a corporate management practice based on modern and generally accepted principles of corporate

management, experiences and best practices in this sphere, honouring the requirements laid down by applicable regulations, with the respect for the global market conditions and trends on the domestic telecommunications market and defined developmental goals of the Company.

The Company Supervisory Board is competent for the application and interpretation of the Corporate Management Code (hereinafter: Code), regular monitoring of the implementation of the Code and compliance of the corporate organization and activities of the Company with the Code.

The application of the principle of adequately acknowledging the interests of all existing and potential shareholders, investors, creditors, service users, employees, and members of the Company's bodies, is ensured through the work and decision-making procedures of the corporate governance bodies as defined by the by-laws, through communication and the coordination of activities between all corporate bodies, managers at the business seat of the Company and units of its territorial organization, employees, shareholders and the public.

In implementing the corporate management system, there were no derogations from the rules envisaged by the Corporate Management Code.

SHAREHOLDERS' RIGHTS

All shares of the Company are ordinary shares and each share grants a right to one vote in General Meeting sessions.

The right to personally participate in General Meeting sessions and debates on all issues on the agenda, including the right to forward motions, ask questions pertaining to the items of the Agenda of a General Meeting session

and receive answers is exercised by the shareholders with at least 1.0% of the total number of the Company shares and/or their proxies who represent at least 0.1% of the total number of the Company's shares.

The introduction of the aforesaid census for personal attendance of a General Meeting session resulted from the fact that there is a very strong corps of the shareholders of the Company (more than 4.8 million). In such conditions, insisting on a census in line with the Articles of Association is imperative because its absence might affect the efficiency and rationality in the process of organizing and holding a General Meeting session.

Naturally, the aforementioned census does not restrict the rights of the shareholders that individually hold less than 0.1% of the total number of shares of the Company to participate in the work of a General Meeting session through a joint proxy or to vote in absentia.

The Company is guided by the principle of an even-handed and equitable treatment of the shareholders and, in that regard, it takes measures which, *inter alia*, ensure:

- timely and regular receipt of all relevant updates about the Company in accordance with the obligations laid down by applicable regulations (including information available on the Company's website),
- participation and voting at General Meeting sessions,
- timely, accurate and full provision of information of special importance for the operation of the Company, pertaining to important corporate changes (particularly amendments to the Articles of Association, capital reductions or increases, significant changes in the ownership structure, status changes and changes in

the legal form and disposal of high value assets,

- deciding on the election and dismissal of Supervisory Board members,
- determining remunerations for the persons elected to the Supervisory and Executive Boards of the Company,
- ensuring an even-handed treatment of all shareholders (including minority shareholders).

The Company endeavours to encourage the shareholders to participate in the work of the General Meeting and in that regard:

- it schedules General Meeting sessions in time to provide for the shareholders to familiarize themselves with the Agenda of the General Meeting and prepare for participation in a session,
- envisages a mechanism of the shareholders' in absentia vote so that personal vote and in absentia vote have an equal effect.

All relevant information and material for a General Meeting session, including power of attorney forms and in absentia vote forms are available on the Company's website www.telekom.rs, within the legally prescribed deadlines before the holding of the General Meeting session.

In view of the fact that there are a large number of shareholders, the Company frequently uses its website to communicate with the shareholders.

SUPERVISORY BOARD

The Supervisory Board performs the tasks from its scope of responsibility in accordance with the applicable regulations, the Articles of Association of the Company and the Rules of Procedure of the Supervisory Board, in a bid to act in the Company's best interest.

The Rules of Procedure adopted by the

CORPORATE MANAGEMENT

Company Supervisory Board regulate as follows: organization, the method of work, including the deadlines and manner of submitting the material for a session to the Supervisory Board members, the method of drafting and content of the minutes, the voting procedure (quorums for the holding of sessions and decision-making) and other issues of importance for an efficient operation of the Supervisory Board.

The Supervisory Board includes 7 (seven) members elected by the Company General Meeting, whereof one is independent from the Company in terms of applicable regulations (an independent member of the Supervisory Board), and the chairman is elected by the Supervisory Board from among its members, by a majority vote of the total number of Supervisory Board members, at the proposal of the Supervisory Board members nominated by the controlling shareholder of the Company. When putting up candidates for the chairman of the Supervisory Board, the Supervisory Board members nominated by the controlling shareholder are guided by the principle of candidates' excellence on the professional and personal planes and in terms of the trust placed in them by the shareholders and other Supervisory Board members.

The Supervisory Board set up an Audit Commission of the Supervisory Board of the Company (Decision no. 380052/6 of 13 December 2012), which takes activities and actions in accordance with the competences laid down by legal regulations and the aforementioned decision on its set-up. The said decision, *inter alia*, specifies as follows: a quorum and the manner of holding a session of the Audit Commission, its composition and mandate and Commission members' right to remuneration. The Commission is answerable to the Supervisory Board and informs it about the tasks and activities it takes, at least twice a year, and any time the Supervisory Board requests that such reports be submitted.

EXECUTIVE BOARD

The Executive Board consists of 7 (seven) members. The executive directors are appointed by the Supervisory Board and one of the executive directors authorized to represent the Company is appointed as the director general of the Company by the Supervisory Board. When electing the executive directors, the Supervisory Board takes into consideration their professional, organizational and personal qualities and when electing a director general, it is guided by the candidate's organizational abilities which are particularly reflected in an efficient organization of the Company's business operations and activities of the Executive Board and coordination of the work of Executive Directors. The organization, method of operation and decision-making of the Executive Board are specified by the Rules of Procedure adopted by the Executive Board in line with its legal and statutory competences.

REMUNERATION AND REWARDS FOR MEMBERS OF THE CORPORATE GOVERNANCE BODIES

The General Meeting passed Decision No. 117294/12 of 20 April 2012 determining the remunerations paid to the chairman and members of the Supervisory Board (with amendments No. 203325/11-2013 of 27 June 2013) and Decision No. 117294/13 of 20 April 2012 on determining the remuneration policy for the work of the executive director appointed as director general and other executive directors of Telekom Srbija a.d. (including the employment contracts of the director general and other executive directors) (with amendments No. 203325/12-2013 of 27 June 2013). The Supervisory Board passed Decision No. 380052/6 of 13 December 2012 on setting up an Audit Commission of the Supervisory Board of Telekom Srbija a.d. whereby, among other things, it stipulated the right to remuneration for the chairman and members of the Commission.

INTERNAL SUPERVISION AFFAIRS

Set up within the Company is an organizational unit in charge of internal supervision affairs (under the name of: Internal Audit), which controls the compliance of the Company's operation with the law and other regulations and by-laws of the Company. Internal supervision pursues the activities in the domain of internal supervision which include: inspection of the compliance of the Company's business operations with the law, other regulations and by-laws of the Company; supervision over the implementation of accounting policies and financial reporting; control of the implementation of the risk management policies; monitoring of the compliance of the Company's organization and activities with the code of corporate management; evaluation of the policies and processes in the Company and forwarding proposals for their improvement. The head of Internal Supervision regularly informs the Audit Commission of the audit of business operations. In its by-laws, the Supervisory Board regulated the method of conducting and organizing the activities of the internal audit of business operations, including the terms to be fulfilled by the persons performing the tasks of internal audit of business operations, as regards professional knowledge or expertise, experience and respect for ethical norms which make them suitable for the performance of said tasks in the Company.

In its decision No. 152744/18-2013 of 23 May 2013, the Supervisory Board adopted the Internal Audit Charter which is necessary for ensuring independent and objective functioning of the organizational unit in charge of internal audit affairs, which regulates the purpose, authorizations, duties and responsibilities of all participants in the performance of work, the method of performing work and other issues related to the Company's internal audit. Besides, the Supervisory Board also adopted the Rules on Internal Audit in Telecommunications Company Telekom Srbija a.d. (No. 152744/17-2013 of 23 May 2013), which

established the principles to be observed by the persons pursuing the audit activities.

COMMUNICATION WITH THE PUBLIC, DISCLOSURE OF INFORMATION AND TRANSPARENCY

The Company ensures the transparency of its operations with compliance of all envisaged obligations in terms of reporting and publication of accurate and complete information and the respect for the principle of providing regular and timely information on the Company's website. The shareholders and the public, primarily by way of the Company's website, report on the financial results of the Company and all important events regarding the Company for which the obligation of such reporting is laid down by the applicable regulations and by-laws of the Company.

OTHER ACTIVITIES IN THE APPLICATION OF THE CODE

The Company is investing maximum efforts in the permanent promotion of the corporate system which will guarantee the actions of all corporate bodies, their members, employees and the Company as a whole, in accordance with the rules of the Code, particularly in the domains which regulate:

- personal interest and the obligation of avoiding the conflict of interest
- cooperation between the corporate governance bodies
- curbing and prevention of bribery and corruption
- engagement of external consultants
- business ethics.

This statement represents an integral part of the Consolidated Annual Statements of the Company's operation for 2013.

BUSINESS OPERATIONS



STRATEGY

BACKGROUND

Telekom Srbija holds a unique position on the Serbian market of telecommunications and multimedia as an operator which offers to its customers exclusive and integrated customer experience based on the provision of the widest spectrum of convergent services. Telekom Srbija plans to maintain a leading position in several market segments through the innovative product and service upgrades by increasing the satisfaction of the customers and business partners and generating the operating revenue growth.

STRATEGIC GOALS

The strategic goals of Telekom Srbija expressed as the company vision and mission clearly point to the high-level business ambitions that are reflected in the aspiration for further growth and development and retention of a leading position on the convergent market of electronic communications, including the multimedia and ICT services.

VISION

We are striving towards enriching and making more beautiful people's lives providing for them global links and extraordinary communications as the regional leader in the information society of the future.

MISSION

New services we are introducing, technologies we are implementing, every change of ours and continual adjustments are intended for our customers, their needs for communication and entertainment, with our employees as a driving force, to the satisfaction of our shareholders.

The accomplishment of business objectives in

a strong competitive environment is supported by the continued engagement of the management and employees in the promotion and strengthening of organizational efficiency in accordance with changes in the environment.

BUSINESS STRATEGY

Telekom Srbija aspires towards promoting the efficiency and effectiveness of its operations through an integrated and convergent model of organization and operation. A change in and the growth of customer needs are supported by the additional innovative development of networks and services.

Telekom Srbija is continuously strengthening its competitor capacity, analysing the trends and development of the technological base, economic environment and customer affinity. Further development of commercial service packages and the promotion of the service portfolio will pave the way for and secure the prospects of the market leader. Srbija will lend support to overall economic recovery and further development, backing other segments of the business environment, thus expanding its business activity and recognisability.

- On the fixed telephony and data market, thanks to its comparative advantages, Telekom Srbija will upgrade the quality of its services and offer to its customers a unique customer experience, attractive and affordable service packages meeting the customer needs and thus retain the leading position on the market.
- On the mobile telephony market, thanks to its comparative advantages, Telekom Srbija will strengthen the customer base, generate the revenue increase and retain the position of a preferred operator with a recognizable ratio between the price and quality of the services rendered by an innovative approach, improvement of the existing and introduction of new services and technologies, upgrading the

BUSINESS OPERATIONS

service quality and provision of a unique customer experience.

- On the market of broadband services of the fixed and mobile networks, Telekom Srbija will endeavour to maintain further growth of its customers and revenues, focusing on an increase in the quality of its services, coverage and availability through combined fixed and mobile offers.
- On the Pay TV and multimedia market, Telekom Srbija will endeavour to increase its market share with an adequate offer of video content and services available on any type of devices and adjusted to the customer's personal needs, with the highest level of service quality. The commercial aspect will stress the value of the services rendered as opposed to the offer of its competitors.
- On the on-line market, Telekom Srbija will endeavour to improve the customer experience and provide for an increase in revenues from advertising, e-commerce, electronic and mobile payments by implementing a unique, upgraded portal.
- On the ICT service provision market, Telekom Srbija will endeavour to become a respectable market player by expanding its service portfolio and generating additional revenues. By improving its organizational model, Telekom Srbija will be able to take advantage of the opportunities offered as a result of convergence of traditional telecommunications markets and IT markets into a single market. By establishing strategic partnerships and acquisitions and enhancing own capacities, Telekom Srbija will offer to the business segment some high-quality solutions that meet the current technological trends and satisfy the customer needs.
- On the market of OTT services, Telekom Srbija will endeavour to maintain its

revenues and market position by analysing the competitors' activities, developing its own OTT applications, introducing new service platforms and establishing partnerships with the OTT providers.

- On the commercial level, by optimizing the company brands, Telekom Srbija will invest additional efforts in ensuring that its customers more clearly recognize the values and functionalities of an integrated market and sales. Customer support will be more adequately adjusted to the needs in all market segments.
- Telekom Srbija will continue to promote its market position through continued improvement of its network and services as an integrated operator, with special emphasis on service innovations in accordance with customer needs and at acceptable prices.
- Telekom Srbija will optimize the sales channel structure managing the relations with customers through the most profitable channels for the purpose of strengthening the customer base and increasing the customer satisfaction.
- Telekom Srbija will continue to gradually integrate its operations, systems and the network towards full IP convergence in order to be able to offer a fully converged product portfolio.

For the purpose of achieving the necessary level of financial vitality, in accordance with the shareholders' expectations, Telekom Srbija will focus on the promotion of internal processes and the accompanying metrics.

IMPLEMENTATION OF THE STRATEGY

The accomplishment of strategic objectives and the implementation of the strategic business plan are supported by the introduction of organizational competences with the aim of improving decision-making, efficiency and

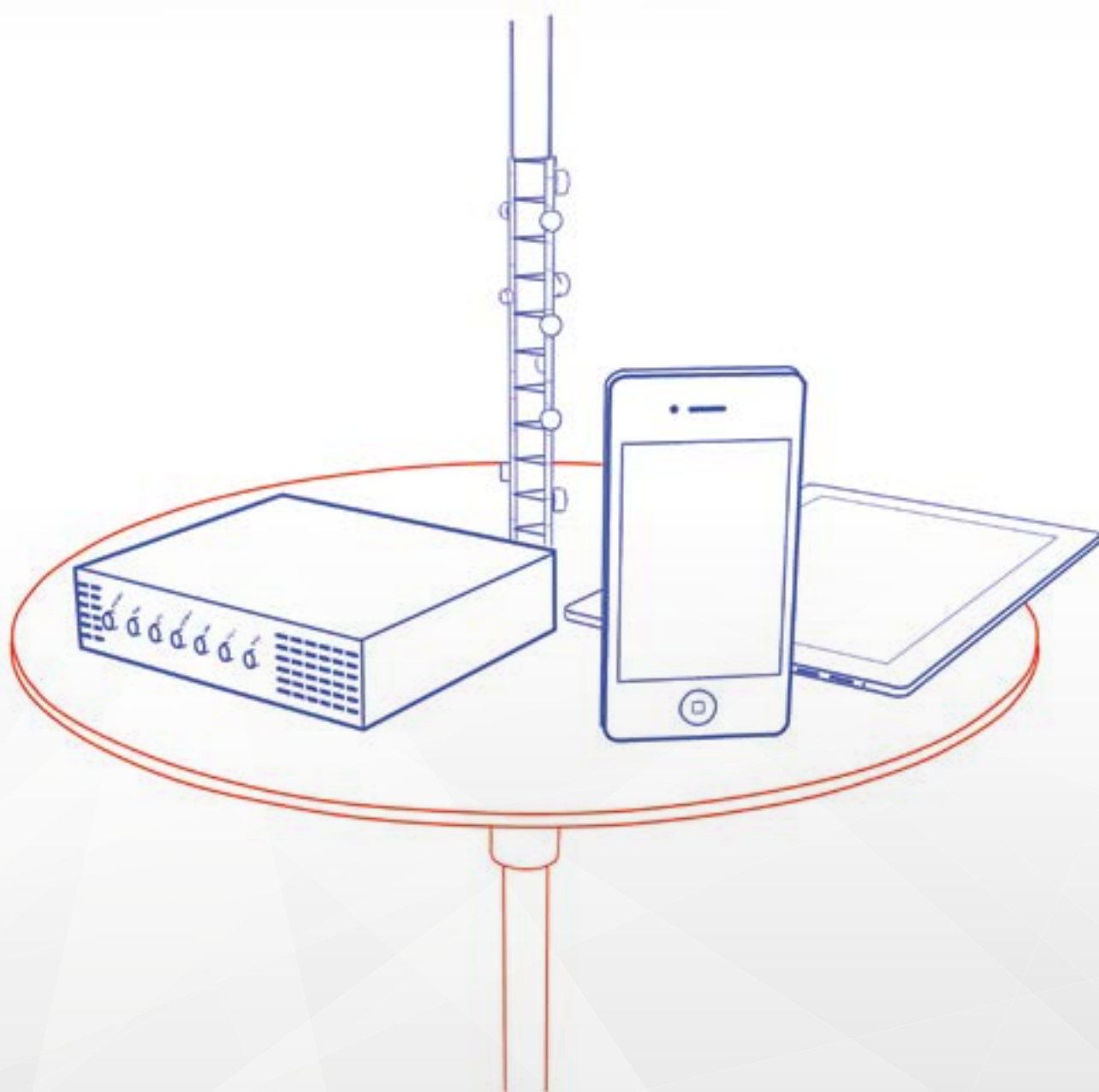
metrics in the Company. Telekom Srbija bases the implementation of the strategy on the continuity of development and application of strategic initiatives, acknowledging the market momentum and the need for constant change from within, analysing changing customer needs, the activities of competitor companies and the expectations of the shareholders and a broader social community.

PREPARATION OF A NEW STRATEGIC BUSINESS PLAN OF TELEKOM SRBIJA

In mid 2013, Telekom Srbija launched the preparations for drafting a new Strategic Business Plan (SBP) that will integrate the planning activities for the time period of 3 years. The key segments of corporate strategy, the strategic guidelines for the key segments of the corporate strategy and the structure of the content of the new Strategic Business Plan have already been defined.

In late October 2013, a project was launched for the preparation of a new Strategic Business Plan of Telekom Srbija for the 2014-2016 period with the support of an internationally recognized consulting firm.

BUSINESS OPERATIONS



SERVICES

Telekom Srbija, the leading telecom company in the region, offers to its customers a wide range of services: mobile and fixed telephony, Internet, multimedia, data transmission.

The Company strives to respond to numerous requirements of its customers' and remain competitive in the market by targeting the launch of new services while keeping the pace with continuous technological development in this sphere.

Business Customers

Aimed at meeting the business customers' needs and making the Telekom Srbija's offer complete, a new antivirus protection service was launched in the first quarter of 2013, enabling its customers to use larger number of antivirus software products for all types of customer equipment and data.

In February 2013, new Internet tariff packages (NET packages) were introduced for residential and business customers with the bitrate of up to 5/1 Mbps, 10/1 Mbps, 20/1 Mbps, 30/2 Mbps, 50/2 Mbps and 100/2 Mbps.

In March 2013, BOX 3 and BOX 4 service packages were introduced, intended for SOHO users including fixed telephone connection, asymmetric Internet access, mobile telephone line and/or basic open IPTV package for business customers.

In August 2013, business customers were offered the new Wifi BUS service as the complete solution enabling the customer to buy MiFi device (WiFi modem with GSM module and SIM card) together with chosen WiFi Bus packages.

The CCaaS (*Contact Centre as a Service*) service offers to business customers the complete

outsourcing solution for Contact and Customer Centres using the infrastructure of Telekom Srbija Contact Centre with optional engagement of the staff employed with the Company.

In the sphere of mobile communication package, the Mobile Net Packages service has been launched applying the cutting-edge methods of providing the service to customers based on E2E QoS system for FUP (*fair user policy*). The customer that has consumed free traffic within the package is not charged for the exceeded free traffic quota, such customer is allowed instead to continue the free-of-charge use but at lower bitrate of 64kb/s.

In September 2013, the wavelength leasing service was launched in the sphere of data transmission services enabling connection of various customer locations on the OSI model first layer and fast data transmission via DWDM technology. Point-to-point network topology is applied in long distance locations. The service is intended for business customers and mostly used for connecting data centres i.e. SAN networks aimed at the implementation of *Disaster Recovery* solution.

In order to improve selling of the services to business customers, BlackBerry BES 10 service has been launched, applying BlackBerry 10 platform and new BlackBerry 10 operating system, which facilitates the control of not only BlackBerry 10 *smart* telephone, but also of telephones with some versions of Android and IOS operating systems. The service offers a new possibility of separating private and business environment on the very phone.

By the end of 2013, the service of Nomadic BizFon connection was launched for calls in national and international traffic via the Internet, using the appropriate client software. Nomadic BizFon connection is a part of BizFon group.

By the end of the year, due to the large number of interested customers, the e-Data service was

BUSINESS OPERATIONS

introduced providing access to the data stored in the public telephone directory and to the data located on the portal 11811.rs to the business customers with the specific requirements in terms of using some or all publicly available databases for establishing contact and communication with Telekom Srbija customers in accordance with privacy and electronic communications regulations.

Residential Customers

Within the X Factor partnership project, the X Factor add-on was introduced, enabling the customers to watch the exclusive *live stream* contents and galleries from the X Factor serial. The contents include audition recordings, presenting news, voting, feature stories from show recordings, etc. There are 3 levels of accessing the contents within the add-on.

After launching the *Fair Usage Policy* (FUP) functionality, the *mt:s prepaid* and *postpaid* customers have been offered the unlimited Internet. The users can *surf* the Internet at maximum bitrate as long as they have data quota; after the data quota has been consumed they can use the Internet free of charge at lower bitrates (64/32 kb/s).

The Farm Android App enables the user to watch broadcasting of the fourth reality show, the Farm. This app works on Android-supported devices – version 2.1 or more advanced version. The farm live app could be downloaded by our all private *prepaid* and *postpaid* customers. The app was commercialized in April 2013 and finalized in July of the same year when the show finished.

Since June 2013, mobile telephony customers have been provided with a redesigned *mt:s* Android Apps Centre offering new possibilities and services such as TV channels free *streaming* via an app which enables the users to watch the program on 7 channels via mobile

network: *RTS 1, RTS 2, Prva Srpska Televizija, Pink, B92, B92 info, Studio B*, the customer network service and an option to recommend the app.

In July, the Web TV service was launched enabling the users to access various Internet contents (TV channels, Video clips, etc.) and now it is an independent service available to all Internet users.

In 2013 *KlikSport* portal, which enables the users to watch live exclusive sporting events on computers, included the ABA League (the Balkan-wide regional Adriatic League) and the *Jelen Super League* (the local football league).

HBO GO is a video-on-demand multimedia service (sVOD) which enables the IPTV subscribers to access movies, series, documentary contents and original HBO production via desktop computers, tablets or *smart* phones (iPhone and Android devices).

The *Upload Booster* service offers the customers Net 20, Net 30, Net 50 or Net 100 packages to increase the *upload* rate up to 5, 10 or 15 Mb/s depending on the Net package used. In December 2013 the Express top-up service was changed so the users now get *rsd* 60 credit instead of *rsd* 40. The users that have three top-ups in the last year are entitled to use the service.

mMarket is a virtual shop of Telekom Srbija where all customers, both *prepaid* and *postpaid*, can buy or download for free various multimedia contents for mobile device. mMarket officially started in 2013, and at the moment it is available only in *wap* version. Purchase is available to all users that have registered *MojTelekom* account, where either the monthly bill for *postpaid* users is charged or the credit for *prepaid* users is reduced.

BUSINESS OPERATIONS



INVESTMENTS

In order to retain the Telekom Srbija leading position in the Serbia's telecommunications market, the investment was made in the amount of RSD 13 billion, which is 5% more than in the previous year.

The investments were made in technical development and creating the network flexibility and reliability for regular operation of service platforms resulting in better quality of services offered to our customers and in retaining the existing competitive advantage.

The Company allocated 73% of funds for investment in technical development of network, whereas 27% of total funds were invested in IT and logistics support.

Investments

In million RSD	2013	Growth rate	2012
Technical investments	9.495	-6,3%	10.134
Infrastructural investments	3.449	56,5%	2.204
Total	12.944	4,9%	12.339

Significant investments were planned in all business segments. In 2013 the development of technical investments was directed to the following activities:

- In fixed telephony the investments were mainly intended for upgrade and expansion of access network providing the services on modern *Broadband* (BB) access

to users. The network upgrade has eliminated the old systems and increased the number of users that have been offered modern and high-quality services. In 2013 digitalization reached 99.50% (in 2012 it was 99.11%).

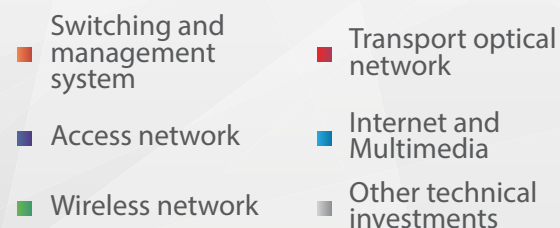
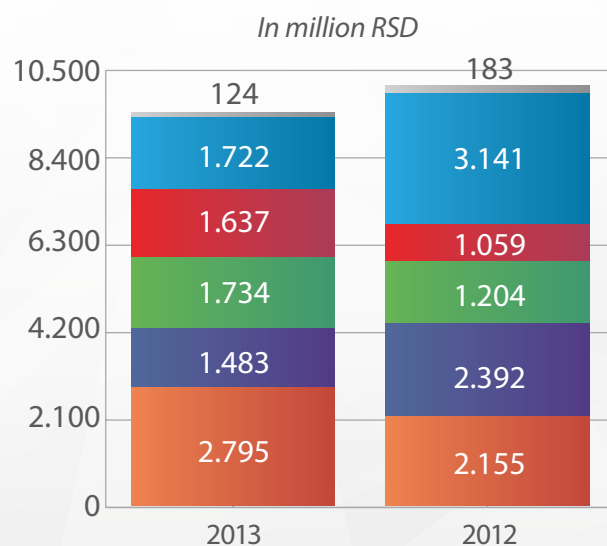
- In mobile telephony the investments were directed to expansion of network in terms of capacities, coverage and also of territory and population. The core network has been upgraded aimed at creating the conditions for an increase in package and voice traffic. In 2013, the expansion of RAN network was continued. The GSM signal territorial coverage was 82.05%, whereas the population coverage amounted to 87.55%. The UMTS signal territorial coverage was 72.34%, whereas the population coverage amounted to 80.15%.
- In the Internet sphere, investments were directed towards expansion of the national IP/MPLS network and of the multiservice network. In 2013 the total number of ADSL ports increased by 7%, which resulted in an increase of free capacity by 12.5%.
- In the sphere of multimedia services, investments were directed towards expansion of *Headend* and *Middleware* platforms.

As for investments in the technical capacities of the telecommunications network, most of the investments in 2013 by the Company were made in the access network (29%), Internet and multimedia (18%), transport optical network (18%), and switching management systems (17%) and wireless network (16%).

BUSINESS OPERATIONS

Technical investments

In million RSD	2013	Growth rate	2012
Switching and management system	1.637	54,7%	1.059
Access network	2.795	29,7%	2.155
Wireless network	1.483	-38,0%	2.392
Transport optical network	1.734	44,0%	1.204
Internet and Multimedia	1.722	-45,2%	3.141
Other technical investments	124	-32,1%	183
Total	9.495	-6,3%	10.134



In 2013, the investments in infrastructure were realized in the amount of RSD 3.4 billion. Infrastructural investments have been mainly made in IT (54%).

In million RSD	2013	Stopa rasta	2012
IT investments	1.857	97,1%	942
Investments in logistics support	1.592	26,2%	1.262
Total	3.449	56,5%	2.204

Infrastructural investments

The most important projects in this period include the replacement of prepaid platform, expansion of the *Billing* system, replacement of the Printing Centre equipment, national interconnection settlement system and the equipment for *Cloud Computing Management* platform.

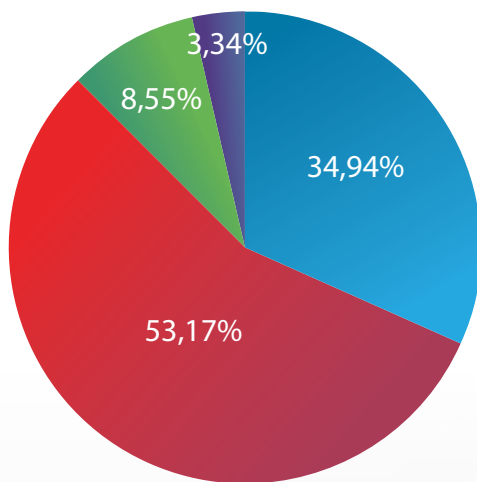
The logistics support investments were primarily made in reconstruction and installation of radio base stations, refurbishment of premises, procurement of power generating units and work equipment. The supply of 334 vehicles has been contracted for undisturbed development of the work process in the Company. By the end of the year, the reconstruction of the office building owned by the Company has begun.

CUSTOMERS

Despite the challenges of fierce competition, Telekom Srbija has a considerable number of customers³ both in fixed and mobile telephony and increasing number of Internet users.

The graph below shows the structure per services.

Structure of customers per service type



- Fixed telephony
- Mobile telephony
- Internet
- Multimedia

Fiksna telefonija

Fixed telephony customers

In thousands	2013	Growth rate	2012
POTS	2.687	-1,9%	2.738
ISDN	69	-7,7%	75
Other*	8	25,0%	7
Total	2.764	-2,0%	2.820

*IP Centrex, Business trunking i E1

3. Active connections/customers at the year-end

At the end of 2013 the Telekom Srbija fixed telephony services were used by 2.8 million customers. In 2013 the Company recorded 2% decline in the number of customers vs. 2012 due to, inter alia, alternative forms of communication such as mobile telephony and the Internet.

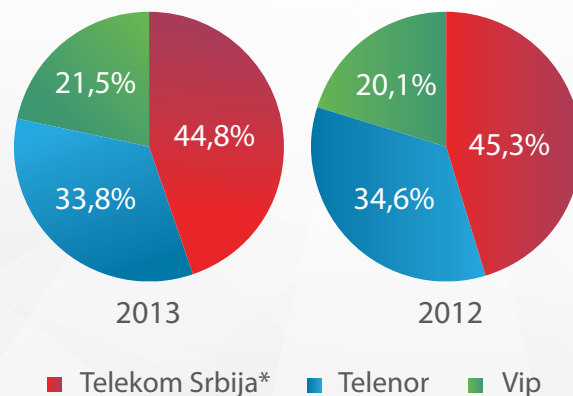
Mobile Telephony

Mobile operators share

Market share*	2013	2012
Telekom Srbija**	44,8%	45,3%
Telenor	33,8%	34,6%
Vip	21,5%	20,1%

*The data are prepared on the basis of the Report of mobile operators

**Active connections at the end of the period are shown



Mobile operators share

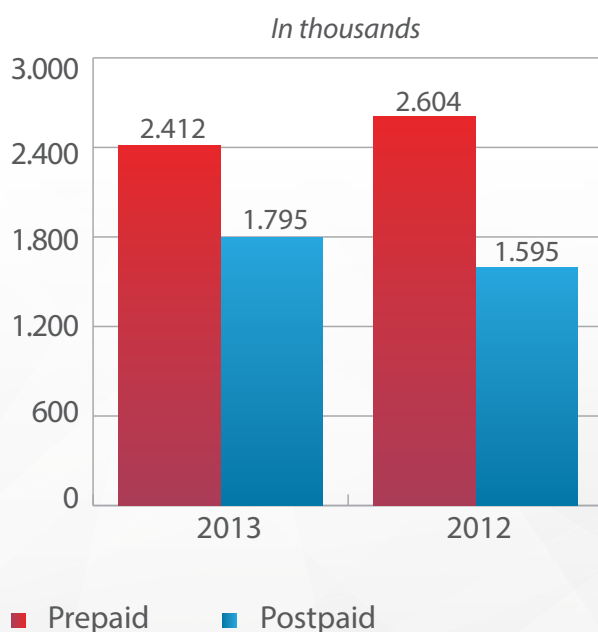
The Company retained its leading role on the market in 2013, with 45% market share.

BUSINESS OPERATIONS

Mobile Telephony Customers*

In thousands	2013	Growth rate	2012
Prepaid**	2.412	-7,4%	2.604
Postpaid	1.795	12,5%	1.595
Total	4.207	0,2%	4.199

* mobile Internet users are included
 **active users over the last 3 months of the observed year



In 2013, the total number of mobile telephony customers increased vs. 2012 as a result of a larger number of *postpaid* customers. Certain number of prepaid customers migrated to postpaid, due to the attractive offer of phones in mt:s packages, or opted for a convergent (Box) package.

Mobile Internet Customers (USB)

In thousands	2013	Growth rate	2012
Prepaid	32	24,1%	26
Postpaid	61	20,7%	50
Total	93	21,8%	76

Mobile Internet customers (USB)

The mobile Internet users, shown within *pre-paid* and *postpaid* mobile telephony customer segments, recorded an increase of 22% vs. 2012. At the end of 2013, the Company had 93 thousand users of the mobile Internet via USB modem.

Internet and Multimedia

Internet and Multimedia customers

In thousands	2013	Growth rate	2012
ADSL retail	550	7,4%	513
ADSL wholesale	126	-1,4%	128
IPTV	244	36,9%	178
Web TV*	20	24,0%	16
Total	941	12,7%	835

*number of subscriptions

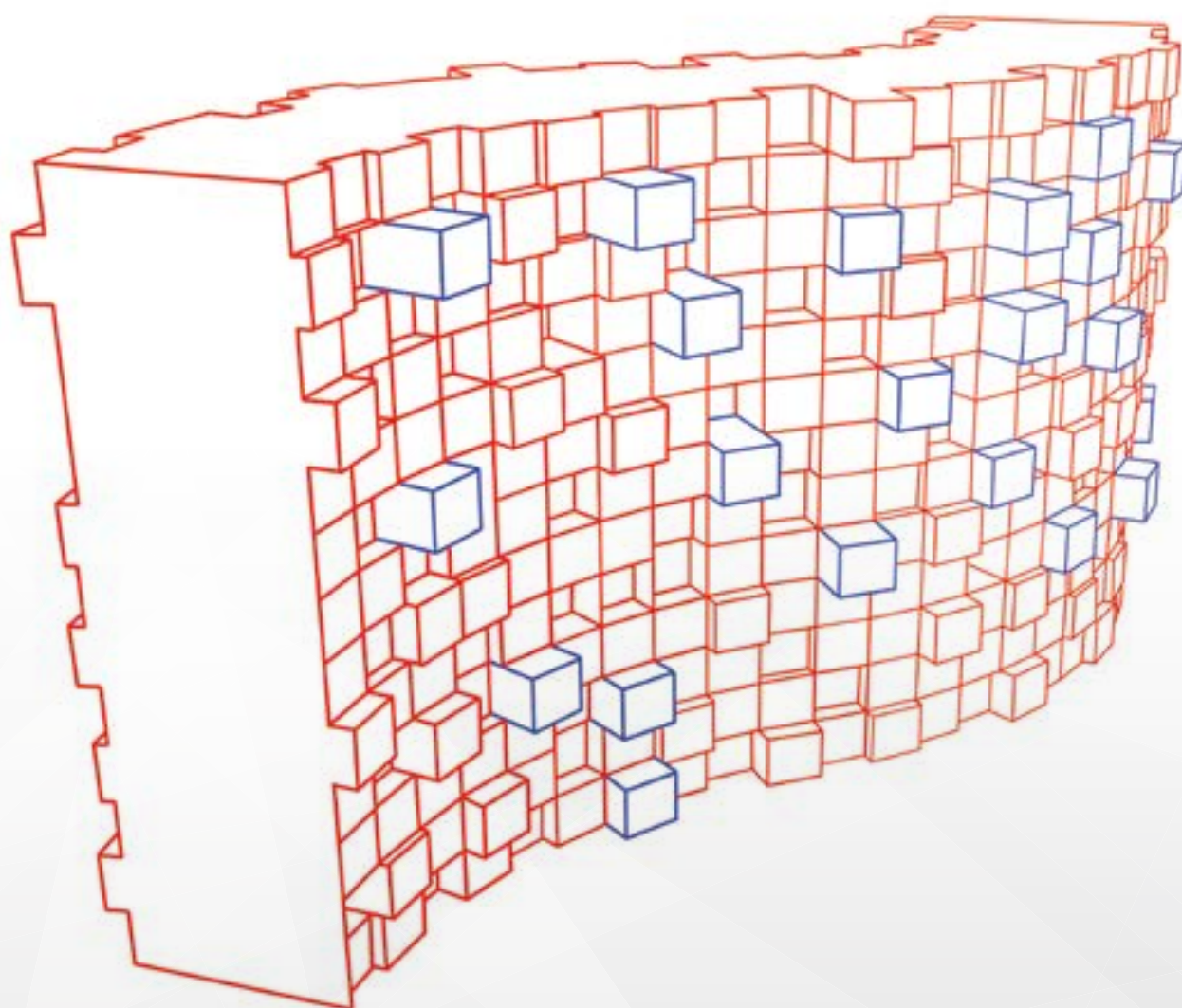
On the Internet market, there is a growing number of customers demanding the broadband Internet, which indicates their need for the service that provides high quality and easily available contents.

At the end of 2013, the Company recorded 550 thousand ADSL retail users, which accounts for 81% share of the ADSL Internet market.

Compared to the previous year, the Company recorded 7.4% increase in ADSL retail users.

In 2013, a considerable growth of IPTV users (37%) was recorded, resulting from the convergent packages offering. The Company recorded 244 thousand IPTV users.

EMPLOYEES

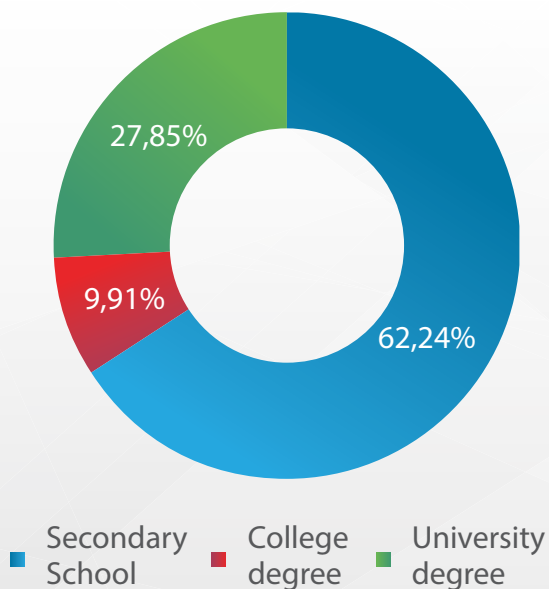


EMPLOYEES

The management and development of human resources is one of the Company's topmost goals and tasks. A care about employees involves care about the overall satisfaction of employees, boosting their motivation and adherence to the Company. Telekom Srbija always strives to ensure for its employees a better future, adequate working conditions, equal treatment of employees, safety at work, health care and possibilities for further advancement and education.

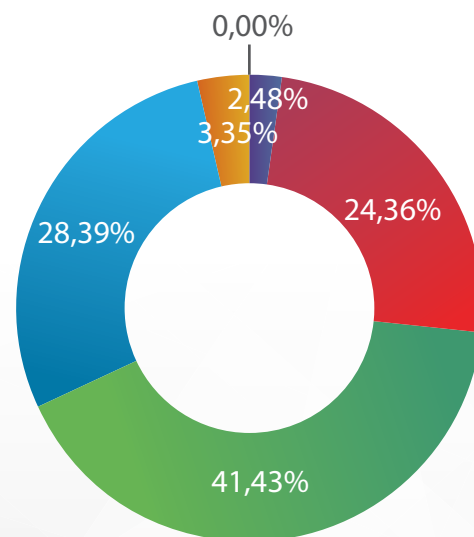
The graph below shows educational structure of employees.

Qualification structure of employees



Age structure of employees

Age	Employees	Percentage
up to 20 years of age	0	0,00
20 to 29 years of age	225	2,48%
30 to 39 years of age	2214	24,36%
40 to 49 years of age	3765	41,43%
50 to 59 years of age	2580	28,39%
60 and more y. of age	304	3,35%



- up to 20 years of age
- 20 to 29 years of age
- 30 to 39 years of age
- 40 to 49 years of age
- 50 to 59 years of age
- 60 and more y. of age

EMPLOYEES

Jubilee Awards

The jubilee awards are granted to employees and ex-employees, who complete, in the period 2 June of the previous year – 1 June of the current year:

- 10 years of uninterrupted employment with Telekom Srbija;
- 20 years of uninterrupted employment in PTT system of Serbia;
- 30 years of uninterrupted employment in PTT system of Serbia;
- 35 years of uninterrupted employment in PTT system of Serbia.

The awards are granted on the basis of the average gross salary in the Company for the month of June paid to the employees with 20 years of uninterrupted employment in PTT system of Serbia, i.e. ½ of the average gross salary for 10 years, 2 average gross salaries for 30 years and 3 average gross salaries for 35 years.

In 2013 the jubilee awards were granted to 845 employees, as follows:

	Employees	Former employees	Total
Continuous years of service	No. of persons	No. of persons	No. of persons
10	192	0	192
20	264	0	264
30	285	2	287
35	99	3	102
Total	840	5	845

Jubilee awards

Education

EXTERNAL EDUCATION IN THE COUNTRY AND ABROAD

In 2013, a total of 1039 employees were referred to external education in the country and abroad, who had 4,144 training days that accounts for approximately 4 days per attendee.

The external educational events in the country were attended by 682 beneficiaries, whereof 225 employees were sent to referential seminars, 126 to trainings and seminars, 17 to law-mandatory trainings (safety and health at work), 60 to business skills trainings, and 101 employees to managerial skills courses. The attendees spent 2,195 training days in the country, which accounts for 3, 22 per attendee.

Educational events abroad were attended by a total of 357 employees, whereof 186 attended conferences, congresses and seminars, 115 attended the training in operating the equipment according to the contracts concluded with suppliers, 27 attended forums, 26 attended vocational training and workshops and 3 employees visited fairs. The attendees spent 1,949 days abroad, which accounts for 5.45 per attendee.

The Company enters into contracts with the employees that are sent to training in the country and abroad so that they are bound to stay with the Company for 24 months. The number of employees having the contractual obligation as at 31/12/2013 amounts to 976 (845 for training in the country and 131 for training abroad under the contract concluded with suppliers).

IN-HOUSE TRAINING

In 2013, the Training Centre in the Human Resources Division organized in-house training attended by a total of 325 employees, whereas vocational education was attended

by 59 participants, 106 employees attended professional skills training, 71 employees attended the English course (39 – group lessons, 32 – individual lessons with department managers), and 89 employees had *e-learning* training programs. As for *e-learning* training courses, the employees were tested in the field of IT security and protection. The attendees spent 2238.25 days on in-house training, which accounts for 11.8 per attendee.

The number of internal and external education beneficiaries in the country and abroad totals to 1275.

Schooling

The Company enters into contracts on settlement of mutual rights and liabilities with employees referred to various types of additional schooling, particularly with regard to the period of completion of schooling and the period of mandatory stay in the Company; as at 31/12/2013 there were 60 active contracts (7 for the 1st degree vocational studies, 12 for the 1st grade academic studies, 24 for master studies, 3 for the 2nd degree vocational studies, 6 for MBA studies and 8 for postgraduate, PhD and specialist academic studies). In 2013, 26 new schoolings were approved, as follows: 9 for the 1st grade academic studies, 6 for the 1st degree vocational studies, 4 for master studies, 4 for specialist vocational studies, 2 for specialist academic studies and 1 for MBA studies.

LICENCES, CERTIFICATES, MEMBERSHIPS

In 2013, the Company financed different types of licences, certificates, professional exams and enrolment fees for a total of 679 employees, as follows: the Engineer Chamber membership fee renewal for responsible designer and contractor licenses for 503 employees, acquiring the new licenses for 29 employees, vocational exams for 16 employees, acquiring of CISCO and other vocational certificates for 40 employees, PMI membership fee for 47,

re-certification for 5 employees and taking the PMP exam for 1 employee, the Internal Auditors Association membership for 15 employees, the Association of Accountants and Auditors membership for 20 employees, taking 1 bar examination, the Chamber of Certified Auditors membership for 1 employee and GIAC membership for 1 employee.

KNOWLEDGE BASES

In 2013, the Company's membership in the knowledge bases of international organizations was renewed, as follows:

Gartner Ireland Limited (modules: Gartner Executive Program EXP membership - CIO ESSENTIAL; Gartner for Business Leaders, Program Management & Marketing), throughout the validity period of the Contract no. 218519/14 dated 20/12/2012 (2012-2014)

TeleManagement Forum - NGOSS program, throughout 30/11/2013 – 29/11/2014

Information Security Forum, throughout 1 July 2013 – 30 June 2014

ASSESSMENT OF THE EMPLOYEES' WORK PERFORMANCE – AWP FOR 2012

In 2013, the procedure of assessing the managers' and the employees' work performance in 2012 (second phase) was completed, an internal report on the results was made on the level of the Company, the organizational units and groups of employees, and a preliminary preparation for AWP for 2013 was completed.

Recruitment and selection

In 2013, the Company engaged 136 external candidates of the total of 418 external candidates involved in the selection procedure.

Pursuant to internal advertisements, 15 employees were assigned to new positions

EMPLOYEES

– based on internal selections performed with 209 employees. Pursuant to the analysis, it can be concluded that the number of advertised positions in 2013 was 40% higher compared with the previous year.

PRACTICAL TRAINING

In 2013, practical training in the Company was done by 59 university students and 11 high school students. The implementation of university and high school student practical training was regulated and innovated by the *Guidelines for organizing practical training of university and high school students in the Company and granting scholarships for talented students*.

An Agreement on Cooperation was signed with the University of Belgrade and the following higher education institutions: the Faculty of Organizational Sciences, the College of Vocational Studies for Information and Communication Technologies, the College of Vocational Studies for Electrical Engineering and Computing and the Vocational College for Entrepreneurship in Belgrade.

Within the recruitment of young talents, an Agreement on Cooperation was signed with the Ministry of Youth and Sports that allows the beneficiaries of the Fund for Young Talents to do a two-month summer practical training in the Company, which will facilitate their transition from formal education to practical engagement.

Employees' benefits

IMPLEMENTATION OF THE POLICY OF MATERIAL, SOCIAL AND HEALTH PROTECTION OF EMPLOYEES

Collective Insurance Program

All employees in the Company are insured from the consequences of accidents, severe illnesses and surgeries, at work or outside of work (24x7), with additional insurance of

employees who are assigned to work posts entailing higher risk.

The program is implemented pursuant to the insurance agreements/policies, which the Company concluded in 2013 with the insurance companies *DDOR Novi Sad a.d.o.* in case of accidents and *Delta Generali osiguranje a.d.o.* in case of severe illnesses and surgeries. Pursuant to the concluded insurance policies, the insurance companies reimbursed the insured sums for 322 employees and members of their close families in 2013.

Voluntary Retirement Insurance Program

All employees in the Company are provided with regular monthly payments against retirement contribution for voluntary pension insurance up to the amount of non-taxable amount in line with the Law. The program was implemented according to the agreement on retirement schemes which the Company has concluded with the joint stock companies for the management of voluntary pension funds *Delta Generali a.d.* and *Dunav a.d.* starting from 2007.

Scholarship program for the children of deceased employees

In accordance with the Company's internal by-laws governing the field of monetary aid for the children of deceased employees during regular secondary and university education (scholarships), the Company, based on the contracts concluded in 2013, granted regular monthly payment of scholarships for 117 children of deceased employees.

Solidarity Aid Program and other types of help

In accordance with the Company's internal by-laws governing the field of granting solidarity and other types of aid, the Company paid solidarity aid to a total of 296 employees and

members of their close families on all grounds granting the exercise of such rights.

Aid program for resolving the employees' housing needs

In accordance with the Company's internal by-laws regulating the allocation of housing loans to the Company's employees, some 70 contracts on housing loans were concluded.

SPECIALIST MEDICAL CHECK-UPS, HEALTH REHABILITATION AND RECREATION

With the aim of prevention and improving the employees' health, the Company organized specialist medical check-ups for 2,754 employees, health rehabilitation for 641 employees and recreation for a total of 190 employees.

IMPLEMENTATION OF THE POLICY OF HARMONIZING RELATIONS WITH EMPLOYEES

All employees in the Company have at their disposal expert teams of lawyers, psychologists and social workers in the form of labour, legal and psychological counselling. In 2013, 24 texts were published on the company website – short professional topics and the latest news in the domain of labour law, and 21 answers to the employees' questions were published within the Labour and Legal Counselling section. Within psychological counselling, 53 employees' requests were fulfilled and 11 texts were published on the internal portal within the Psychological Counselling section.

IMPLEMENTATION OF THE POLICY OF INTERNAL INFORMING OF EMPLOYEES

It represents a program of continuous, accurate and timely informing of employees via the Intranet and the Company's Newsletter. The Intranet implies regular and continuous preparation, processing and publishing of information on the internal site My Portal. The posted

information is classified in categories: *ad hoc* information related to important announcements in the field of human resources (employees' rights), information about current events in the company that is posted on a daily basis and information that is posted twice a month (current events in the sphere of culture and sports, telecommunications in the country and abroad, sections Visit Serbia, the World, Famous Serbs, Great Thoughts by Great People, From the Proof-reader's Perspective, Psychological Counselling, Labour and Legal Counselling, Funny Press Clipping, German and English Language Tests, Survey and New Technologies). In 2013, 94,547 single user visits and 2,154,462 single visits were recorded, the corporate Newsletter (a total of 12 issues) was distributed, along with the latest news from the subsidiaries and a presentation of new services and current events in the sphere of culture and telecommunications, and 13 corporate bulletins were issued.

Social activities

Employees' sport contests program

In line with the internal by-laws and in cooperation with the representative trade unions, the Company implemented the Employees' Sport Contests Program in 2013.

Employees' sport recreation program

In line with the internal by-laws, in 2013, the Employees' Sport Recreation Program was financed and implemented pursuant to contracts on the provision of sport recreation services, which the representative trade unions concluded with the service providers.

Gifts for 8 March

On the occasion of March 8, International Women's Day, and in accordance with the Company's internal by-laws, the Company

EMPLOYEES

granted the right to a one-off payment of funds as a gift to women employed/engaged outside of employment agreement.

New Year gift for the employees' children

In 2013, the Company granted the right to a one-off payment of funds – gift to employees/individuals engaged outside of employment contract, for the purchase of New Year parcels for children of up to 10 years of age, on the occasion of New Year 2014, including the organization of New Year shows held in Belgrade, Novi Sad, Kragujevac and Niš.

SOCIALLY RESPONSIBLE BEHAVIOUR

The humanitarian association of Telekom Srbija employees, "From the Heart", organized a total of 45 voluntary blood donation campaigns in Belgrade and all major towns on the territory of the Republic of Serbia. A total of 1,120 employees took part in the campaign, while 46 employees participated in the 4 campaigns of signing donor cards.

RISK MANAGEMENT

In its regular operations, the Company is exposed, to different extent, to certain financial risks, as follows:

- market risk (including the foreign exchange risk, the risk of change in interest rates and the risk of change in prices),
- liquidity risk and
- credit risk.

Risk management in the Company is directed at minimizing potential negative effects on the financial position and operations of the Company in the circumstances of unpredictable financial markets.

Risk management is defined by the financial

and accounting policies of the Company, adopted by the competent corporate management body. In 2013, there were no changes in the risk management policies which are revised in order to reflect changes in the market conditions and the Company's activity.

The risk management policies of the Company are established with the aim of identifying and analyzing the risks that the Company is exposed to by determining risk limits and control, along with monitoring risks and adhering to the established limits. The corporate governance bodies of the Company were founded with the aim of monitoring the way in which the management handles the risks that the Company is facing.

MARKET RISK

Market risk is the risk of change in the market prices such as: foreign currency exchange rates, interest rates and the prices of instruments of capital, which may have a negative effect on the Company's revenues or the value of its financial instruments. The aim of market risk management is controlling the exposure to market risk within the acceptable parameters, while generating optimum yield.

The Company is exposed to the risk of change in foreign currency exchange rates, primarily the euro.

The Company is exposed to risks that due to fluctuations in market interest rates affect its financial position, its operating result and cash flows.

The risk of change in the interest rates is mainly caused by long-term loans from banks and loans from the suppliers with a variable interest rate. As at December 31, 2013 and 2012, liabilities against loans were mostly expressed in euros with a variable interest rate related to Euribor.

The Company performs the analysis of exposure to risk from change in the interest rates on a dynamic basis, taking into account alternative sources of financing and refinancing, primarily for long-term liabilities, since they represent the most significant interest-bearing item.

The Company is not exposed to a significant risk of change in the prices of equity securities.

On the other hand, the Company is exposed to a risk of change in the prices of services because it faces intense competition in the field of mobile telephony, the Internet and multimedia, and the emergence of new operators in the field of fixed telephony, which the Company is trying to make up for by introducing various services.

Apart from that, the Republic Agency for Electronic Communications has imposed, among other obligations, the obligation of controlling the prices in certain markets where the Company was declared an SMP operator.

LIQUIDITY RISK

Liquidity risk is a risk that the Company will not be able to settle its financial liabilities when due. The Company's approach to liquidity risk management is aimed at providing, to the extent in which it is possible, adequate liquidity for settling due liabilities, both under normal and extraordinary circumstances, without incurring unacceptable losses or risk of harming the Company's reputation.

With the aim of managing liquidity risk, the Company has adopted financial policies which define the maximum amount of advance payment to the suppliers of works, equipment and services, the grace period and the repayment period. The Company also tracks the expected cash-ins from receivables, along with the expected cash-outs on grounds of liabilities.

CREDIT RISK

Credit risk is managed by undertaking certain activities and measures on the Company level, such as client risk assessment, monitoring client's operations and its financial situation and managing receivables. In case of a client's failure to fulfill its obligations towards the Company, further provision of services to the client shall be terminated.

There is no significant risk concentration since the Company has a wide base of customers who are not interconnected and who individually have low liabilities towards the Company. Apart from the termination of further service provision, with the aim of securing collection, the Company also undertakes the following measures: debt rescheduling, launching court proceedings, out-of-court settlements, etc.

CAPITAL RISK MANAGEMENT

The Company policy is to provide a sufficient level of capital to maintain the trust of investors, creditors and the market, and sustain further development of operations.

The Company tracks capital based on the debt-to-equity ratio, which is calculated as a ratio between the Company's net debts and its total equity.

REPORT ON CORPORATE AND SOCIAL RESPONSIBILITY



REPORT ON CORPORATE AND SOCIAL RESPONSIBILITY

Companies operating in a socially responsible way represent a specific driver of progress of the entire society. Social responsibility is not just an ethical duty of companies, but also involves mutual understanding between the companies and the community where these companies operate.

Commitment to young people and education, employees, service users, interaction with the shareholders, and integration of social care and care about the environment in everyday operations, represent basic principles on which the business strategy of the Company – Telekom Srbija and its subsidiaries lies.

Telekom Srbija wishes to become a modern regional company in all aspects of corporate management. At the same time, the Company sees itself as a leader among companies in the field of corporate social responsibility (CSR), but not only through the implementation of specific activities, but also through pioneering education in this field.

Apart from the Code of Ethics, adopted in 2003, and the Code of Corporate Management, adopted in 2012, as a basis for the implementation of socially responsible practice and corporate philosophy, within the existing CSR strategy and in the creation of a mid-term CSR draft strategy, the Company was directed by guidelines presented in the following documents: "Strategy for the Development and Promotion of Corporate Social Responsibility in the Republic of Serbia for the period between 2010 and 2015", "Strategy for the Reduction of Poverty", "National Environment Protection Program", "National Strategy for the Sustainable Development of the Republic of Serbia for the period 2009-2017". Also, the document includes the recommendations

and standards of international organizations, such as the European Commission and its "Corporate Social Responsibility Strategy" for the period until the end of 2014, the Corporate Management Principles of the Organization for Security and Cooperation in Europe (OSCE) and the UN Global Compact's principles whose guidelines the Company has been following since 2010, when it became a member of this international network of companies that foster the principles of corporate social responsibility.

Activity frameworks

Having in mind the needs of the environment and respecting the values that the Company advocates, the following frameworks were marked as the key fields of activity within CSR: within the company, through corporate management and work environment; towards the community, through investments into education, health care, culture and art and science; towards the business environment, which involves fostering the relationship with customers, suppliers and the competition; in accordance with nature, by launching initiatives in the field of environment protection, sustainable development and renewable sources of energy.

The Company implements its activities through three forms of corporate social responsibility:

- corporate philanthropy,
- integration into operations,
- innovativeness.

Corporate philanthropy mainly refers to charity activities in the form of donations that do not have a direct influence on business results, but have a positive influence on the company's reputation. Fields that are of special interest to the Company have also been defined as follows: health care, sports, education, religion, humanitarian donations, science, culture and the environment. Apart from the donations, additional

REPORT ON CORPORATE AND SOCIAL RESPONSIBILITY

mechanisms of investment in the community are public competitions and projects of national interest.

Integration of the social responsibility aspect into operations includes all the activities by which the Company, by improving corporate management, is trying to increase the quality of services, responsibility towards business partners, the scope of activities aimed at the reduction of costs, and participation in various surveys important for the Company.

The innovative form of operations involves the implementation of those activities within CSR that create a new environment for mitigating all social problems.

The Corporate Social Responsibility Section within the PR Department, with the logistic support of the PR Section, is in charge of implementing the corporate strategy and all the activities. The Company is also committed to active engagement of all its employees and managers in the implementation of the Strategy guidelines, both through active participation in the implementation within their field, and through initiating projects on the annual level, which will be included in the business plans as a compulsory segment of operations.

The Company continues to further its socially responsible activities, establish partnerships of interest for the community and expand the concept of corporate social responsibility among its employees, and among the business entities with which it cooperates.

From 2011, the Company has been a member of the Business Leaders' Forum, the first network of socially responsible companies in Serbia, which was formed with the mission to encourage the development of corporate social responsibility and establish a lasting and stable practice of social responsibility in the local business sector. Based on its membership, the Company participated in the regular annual activities of the Forum.

In 2013, the Company launched several socially responsible projects, two of which met with a powerful response and had a strong influence on the public.

"Park Your Phone When Driving!" campaign

In accordance with the business strategy and the draft CSR strategy, the Company launched a campaign in November 2013 aimed at increasing safety in traffic with a special focus on the responsible use of mobile phones while driving. Since the Company is trying to ensure that its services are used in a responsible way, the campaign was launched in order to raise drivers' awareness about the dangers of using mobile phones while driving, either for making phone calls, searching the Internet or exchanging SMS messages. In this way, the Company gives up a part of its profit and the advertising of its own services in favor of greater safety in traffic and for the benefit of the entire society.

With an aim of raising public awareness about the dangers of using mobile phones while driving, the Company and its partners, the Traffic Police Department of the Serbian Interior Ministry and the Serbian Traffic Safety Committee, developed all the communication channels – TV video, radio advertisements, online contents, print solutions in the form of billboards and fliers, to ensure that the campaign message reaches every driver. During the campaign, activities were simultaneously organized in four cities – Belgrade, Novi Sad, Kragujevac and Niš where famous sportsmen stopped drivers and gave them hands-free devices, reminding them to responsibly use their mobile phones while driving. The Company also provided hands-free devices for its customers. Namely, 5,000 citizens who showed a valid driver's license at the signing of postpaid contracts got a hands-free device as a gift. At the end of the year, a lecture was held for the students of traffic high schools in

Belgrade, so that the students, as future drivers, would get acquainted with the dangers of irresponsible use of mobile phones while driving. This announced the new, educational phase of the campaign that will continue in the form of lectures and workshops.

"PARK YOUR PHONE WHEN DRIVING" CAMPAIGN IN FIGURES:

- the TV video, as the pillar of the campaign, was viewed almost 100,000 times during the first two months. Many international websites downloaded the video and distributed it further as "The Best Advertisement against the Use of Mobile Phone while Driving". Among the first, the video was shared by the Liveleak website, and in just 14 hours the video was seen by 31,000 visitors;
- the campaign has an active life on social networks – *twitter* and *facebook*;
- In the opinion poll taken by the Serbian Traffic Safety Committee, in cooperation with the Faculty of Traffic in Belgrade:
 - 96% of the 1,000 participants in the poll noticed the campaign and assessed it positively;
 - Of 72% of the respondents who said they had used mobile phones for texting while driving before the campaign, 61% said that the campaign positively influenced their behavior and that they stopped doing so.
- 6,000 hands-free devices were distributed in just two months of the campaign – 5,000 in the outlets and 1,000 during the promotional activities within the campaign;
- during New Year holidays, 150,000 fliers about the campaign in both English and Serbian were handed out at the toll stations throughout Serbia;
- all professional drivers in the Company received hands-free devices and all corporate vehicles were marked with a sticker with the campaign logo.

Having in mind the achieved results and the attention it received in the media, it is clear why the Park Your Phone When Driving campaign won an award for the best non-profit campaign at the Night of the Ad Eaters 2013, and the award for the best TV video, the best socially responsible campaign and the best elements in digital communications, granted by the Market Communications Association.

"City Talking" project

The "City Talking" project was designed and launched to encourage local communities and partners to take an innovative approach to the challenge of improving the tourist offer and communication tools. It was officially launched by presenting the mobile device application "Belgrade Talking", and the application "Novi Sad Talking", which are intended for visitors with the aim of making it easier for them to get around and visit the most important cultural and historic sights in these towns. Innovativeness especially comes into play when using the functionality called Augmented Reality in finding objects. It allows an easy and funny way of accessing basic information about the object described in the application. The Company's partners in this project, the Tourist Organization of Belgrade and the Tourist Organization of Novi Sad, made the application an integral part of the cities' presentation at all fairs, including the largest tourism fair "World Travel Market" held in London.

Based on the example of these two cities, it is planned to make applications for all major cities in Serbia with a defined tourist offer and a significant number of cultural and historical sights that can be presented in this way, and include them in the City Talking project.

REPORT ON CORPORATE AND SOCIAL RESPONSIBILITY

Investment in young people and education

SUPPORT FOR CHILDREN AND MARGINALIZED GROUPS

Investment in the inclusion and socialization of marginalized groups has been one of the main commitments of the Company in deciding about socially responsible projects, from the Company's very founding. There are numerous examples of participation in projects aimed at improving the position of children without parental care. The Company has thus become one of the first partners of the non-governmental organization Center for Youth Integration in the implementation of the "Children's Drop-In Center" in Krfska street.

Investment in sports and popularization of the healthy life style and the true values is one of the main commitments for which the Company has become famous even on the international level. Continuous efforts to include children in sports activities and the promotion of a healthy life style received recognition within the "One Team" project, launched by the prestigious basketball competition "Euroleague". "Partizan One Team Telekom", the project launched in cooperation with the Basketball Club "Partizan", was declared as the best example of work and partnership within the "One Team" program. The program is primarily intended for children without parental care to help them become active members of the community and integrate them into society by means of basketball and the values that practicing sports promotes. The "One Team" project is actually trying to use the power of sports to raise the level of tolerance and help eliminate the public's prejudices towards this social category.

One of the activities in this project was a visit by children from the "Drinka Pavlović" children's home to Telekom Srbija's math camp at Tulba near Požarevac, which is traditionally organized

in order to develop mental and physical abilities in senior elementary school students.

Thanks to cooperation with the "Partizan" basketball club, inmates of the children's home were able to strengthen team work and fair play, spend time with their favorite basketball players and visit the club's matches.

Within support to sport talents, the Company, in cooperation with the Serbian Athlete Association, participated in the project "Children's Athletics", which promotes the introduction of this sport in the classes of physical education in the elementary schools in Serbia. The program involves students from the first to fourth grade. The Company contributed to the implementation of the project by providing specially designed equipment for training adjusted to the children's age. The campaign was implemented in 30 cities throughout Serbia and held under the auspices of the International Athletes' Federation and the European Association of Athletics.

Continuing last year's successful cooperation with the Association of Photographers on the Eye of the Street project, the Company supported the Eye of the City project organized by this association in 2013. The project was launched with the aim of engaging young people from marginalized groups and offering them a chance to turn their experience of living in Belgrade into art photographs. The young people gathered in the sing and dance workshop GRUBB, mostly from the Roma population, were trained and given the necessary equipment and support in taking photos by the association's photographers, while the photographs were displayed at the Artget gallery of Belgrade's Cultural Center.

THIRD MT:S ANDROID™ COMPETITION

As the support for young people and education represents one of the most important spheres of the Company's social responsibility,

a competition for the creation of Android applications was launched in cooperation with the Mathematics Grammar School of Belgrade three years ago. The competition aimed to best connect the core activity of the Company and the entrepreneurship of secondary school students gifted in programming, who thus received an opportunity to practically apply their knowledge obtained in school.

Apart from cooperation with the Mathematics Grammar School, an educational institution of special importance, the third mt:s Android competition also included the Svetozar Marković Grammar School of Niš and the Jovan Jovanović Zmaj Grammar School of Novi Sad whose students were invited to participate. In order to familiarize the students with the basic idea of the competition and the terms and rules thereof, the Company's representatives held presentations in each of the three schools in the course of September 2013.

The experience so far in conducting the competition has revealed that mobile applications are a good platform for students to use their programming skills and express their creative potentials.

As compared to the first competition launched in 2011, the applications which were shortlisted in the second and third competitions attest to a major progress in terms of quality and functionality. Also evident is a much greater interest of students in participating in the competition.

Besides valuable awards prepared by the Company for the three top-ranked teams – the award for the winning team is a visit to the World Mobile Congress in Barcelona, and tablet computers and smart phones for the runners-up – a special incentive for the students is also an opportunity to master practical IT skills and IT-related professions which are in higher demand as regards their future careers. Likewise, the Company ensures the placement

of all functional applications on the mobile application market - Google Play.

THE SUPPORT FOR EDUCATIONAL PROJECTS

A large number of socially responsible activities of the Company are aimed at improving the conditions for the acquisition of knowledge by younger generations.

From among the projects supported in 2013, the most important are: *The Open-Air Geographical Laboratory* in the village of Ripanj, *the Influence of Interactive Exercises on the Development of Students' Abilities (Brain Breaks)* in the Ivo Andrić Primary School of Belgrade, and to mark International Children's Book Day, the Company presented a large number of children's books to the students of the Milun Jakšić primary school in the village of Banje, Kralj Milutin primary school of Gračanica, Sveti Sava primary school in Sušica and Miladin Mitić primary school in the village of Laplje Selo.

The Company supports our national team of knowledge, that is, a team of young talents that brings medals from international competitions in several scientific disciplines. Apart from students of the Mathematics Grammar School of Belgrade, with whom there is partner cooperation, the teams also include representatives of other secondary schools in Serbia.

Thus, this year, students of the Mathematics Grammar School achieved a fantastic result in the Archimedes competition held in Bucharest by winning six medals: four gold and two silver ones. Besides the support for participation in the Archimedes competition in Bucharest, also made possible is the mathematicians' participation in the Mathematics Competition held in Moscow, Euler's Olympiad in St Petersburg and in the prestigious International Mathematics, Physics and Informatics Competition in Kazakhstan in which young mathematicians competed for the first time.

REPORT ON CORPORATE AND SOCIAL RESPONSIBILITY

THE SUPPORT FOR THE ENTREPRENEURSHIP OF YOUNG PEOPLE

Recognizing the importance of promoting education through the development of young peoples' entrepreneurship, the Company has supported the Youth Achievement organization and its project entitled *Business Challenge* for three years now. This project envisages that representatives of the business sector present secondary school students with business challenges – problems to be solved by students during a one-day competition. In the course of 2013, through the engagement of the Company's employees as mentors for students' teams and as a jury, the Company actively supported the holding of the business challenge event in Belgrade.

At the beginning of 2014, the prestigious Virtus award – the most important recognition for corporate philanthropy in the country, was presented for long-term partnership which has been maintained with the Youth Achievement organization for three years now.

CONNECTED WITH STUDENTS

For years now, the Company has maintained successful cooperation with the ESTIEM, AIESEC and EESTEC student organizations, through their local offices in Belgrade. This cooperation is maintained during the scheduled annual events staged by these student organizations, in which the Company's employees volunteer endeavouring to pass to students their knowledge and experiences from the business environment at lectures.

This year's events of student organizations – *Open IT* in the organization of AIESEC and the *Academy of Modern Management* organized by ESTIEM devoted to entrepreneurship are a fine indication that students are interested in acquiring knowledge in the sphere of innovative business ideas and launch of business. During lectures and workshops, the Company's

experts too had an opportunity additionally to familiarize themselves with the stands and views of students and their would-be peers.

Investments in health care

For several years now, the support for health care projects has been a key component of the Company's commitment to invest in the community. Every year, the Company sets aside significant funds for the fitting out and refurbishment of health care institutions, fostering an even regional approach. In this context, special mention should be made of the donations to health care centres providing care for a large number of beneficiaries. The Neurosurgical Clinic of the Serbian Clinical Centre is thus equipped with state-of-the-art surgical microscope which is of exceptional importance for the performance of demanding surgical procedures. This institution performs some 2,500 such operations annually.

Apart from the significant support for the Clinical Centre of Serbia, the Company set aside funds for the University Children's Clinic in Tiršova St for the fitting out of the renovated Abdominal Surgery Ward and the procurement of a portable ultrasound device for diagnosing the musculoskeletal diseases and injuries in children. In the past period, in the form of in-kind donations, the Company also provided free IPTV services on the public premises of the Clinical Centre of Serbia, the Zvezdara Clinical and Hospital Centre, the University Children's Clinic in Tiršova St, the dr Vukan Čupić Institute for the Health Care of Mother and Child and the Sokobanjska Hospital for Cerebral Palsy and Developmental Neurology. The donations were used for procuring the necessary medical equipment to other health care institutions in Serbia, including the Serbian Emergency Centre, the Cardiology Clinic of the Niš Clinical Centre, the General Hospital of Pančevo, the Health Care Centre in the town of Kuršumljija, the Health Care Centre of the town of Kosovska Mitrovica and the Basic Rehabilitation Centre of Kosovska Mitrovica.

The support for culture and science projects

Being confident that art and science must rely on the support from the business sector, the Company supports annual projects and events in the sphere of science and culture which are of national significance. The legacy of one of the most distinguished internationally-acclaimed scientists Mihajlo Pupin, who is meritorious for the invention of exceptionally important patents in the sphere of telecommunications, is most certainly the sphere to which the Company wishes to make its full contribution. In the run-up to the marking of an important anniversary in 2014 – 160 years of the birth of the scientist of Serbian descent, the educational association of the same name and Telekom Srbija launched a string of activities with a single commitment – to affirm his legacy and present the details of his life to the domestic and world publics. The first step to this end was cooperation within the Mihajlo Pupin Virtual Museum project, which pays tribute to this brilliant scientist, inventor and professor. Visitors to the Virtual Museum have an opportunity to learn more about Pupin's life through ten museum sections. At the same time, the Virtual Museum also contributes to a brand new manner of presenting his cultural and scientific heritage. Besides, also provided is access to Pupin's Hometown Complex in the village of Idvor through a virtual walk. After the development of the Virtual 3D Presentation of the Hometown Complex in the village of Idvor, interested visitors may see Pupin's home, school, National Hall, the construction of which was funded by himself, and the nearby church, which all constitute an integral part of this hometown complex. Visits to these museums offer an opportunity to learn important and less generally known facts about Mihajlo Pupin.

Likewise, the Company has been a long-standing sponsor of the Music Scene Masters programme organized by the Ilija M. Kolarac Endowment in Belgrade and the oldest Serbian choral music festival – Mokranjac Days, which, at

the same time, is an important cultural event of the Negotin region. The Festival's programme is based on the recognizable concept of choral performances and the promotion of domestic music creativity. As a loyal friend of the event, Telekom Srbija received a special plaque for its contribution to the organization of the festival in 2013.

Contribution to the preservation of cultural heritage

Since its foundation in 1997, the Company has endeavoured to boost the development of the entire community by supporting the religious communities both in Serbia and in the former Yugoslav countries in which it operates. The Company is recognized as one of the greatest benefactors of St Sava's Church in Belgrade and has contributed to the building of the Church since its restoration in 2001. The digitalization of the Chilandari treasury was one of the key projects within the Company's socially responsible activities.

With its contributions, the Company has participated in the organization of the Fundraising Evening for St Sava's Church and the Church and Parochial Centre of St Paraskeva at Čukarička Padina in Belgrade, supported the publication of the *Svetigora* magazine and Orlić youth magazine, and set aside funds for the Serbian Orthodox Church's stall at the Belgrade Book Fair for years now. Apart from investing in their construction, the Company has also aided the restoration of religious facilities, including the monasteries in Kosovo-Metohija – the Peć Patriarchate, the Monastery of Banjska, the Monastery of Visoki Dečani, the Monastery of Gračanica and the Monastery of Sokolica.

The Company also supports Orthodox sanctities in the region. In the framework of marking the 1700th anniversary of the Edict of Milan, the newly-built Cathedral of the Resurrection of Christ in Podgorica was consecrated. On that occasion, the Company received the Acknowledgement

REPORT ON CORPORATE AND SOCIAL RESPONSIBILITY

as the Grand Sponsor of the Cathedral. The Company backed the marking of the anniversary also by providing telecommunications infrastructure for the TV coverage of a liturgy and an Internet link in the town of Niš. Likewise, the funds were raised for the construction of a fountain in front of the My Place Hotel. The fountain is part of the project entitled *17 Fountains for 17 Centuries of Christianity* launched by the Niš metropolitan municipality of Medijana.

The Company endeavours to meet the needs of religious communities. Thus, to mark the Anniversary, it also supported the Belgrade archbishopric and the organization of the Holy Liturgy at the Čair stadium in Niš. Also provided were the funds for the implementation of cultural projects of the Islamic community.

Responsibility towards the customers

Applying state-of-the-art technological solutions, which ensure communication any time any place, the Company is endeavouring to establish and maintain impeccable communication with its customers and partners. In cases when contemporary solutions do not suffice, responsible companies are expected to make an additional step ahead to accommodate customer needs. Bearing in mind the needs of more than 50,000 our fellow citizens with impaired hearing, the Company launched sign language courses for its employees working in outlets who come into direct contact with customers.

The employees of the outlets in Belgrade, Novi Sad, Bačka Palanka, Zrenjanin, Kikinda, Subotica and Sremska Mitrovica underwent an educational programme tailored to the Company's activity and including some 800 selected gestures grouped into 16 thematic units. Having mastered the envisaged signs and conventional phrases, the employees are able to reply to all questions regarding the telecommunications services without problems. The training was conducted in several phases

and included the total of 45 employees. The Company plans to continue the sign language training in order to include all busier outlets in the country. As well as its employees, the Company treats its customers equally, in a bid to adjust its services to their specific needs. The training of the employees in the sign language was launched in cooperation with the Serbian Association of Interpreters for Hearing-Impaired Persons (UTLOSS).

Volunteering

Telekom Srbija's socially responsible activities are a result of its employees' activities and efforts – their endeavour and work at their workplaces, and their benefaction and humanness. Active within the Company is the From the Hearth (*Od srca*) Relief Association which rallies blood donors among the employees and pensioners of Telekom Srbija. Apart from its core activity, the Blood Donors Association also engages in charity work. Recently, it has launched the activities aimed at promoting organ donation.

The Association has been active in the territory of the whole of Serbia and their members foster, through their activities, the tradition of solidarity with other members of the community. The activities of this Association contribute to the promotion of the Company's social responsibility and raising the awareness of its employees of important social issues such as health and humanness, the improvement of the environment, and the support for a change in the habits as regards the preservation and use of resources.

The *From the Heart Association* has concluded cooperation agreements with the Blood Transfusion Institute of Serbia and the Transfusion Institute of the Military and Medical Academy. Besides the said institutes, the Association established cooperation with other institutions as well, including: the Serbian Red Cross, the Serbian Interior Ministry, the Faculty of Applied Arts and other similar associations in Republika Srpska, the B-H Federation, Montenegro and the like.

During 2013, in a string of activities launched by this Association in Niš, Pirot, Prokuplje, Novi Pazar, Kragujevac, Sombor, Požarevac, Pančevo, Šabac, Smederevo, Subotica, Sremska Mitrovica, Čačak and Bor, 1,026 units of blood were collected.

Environment protection report

The strategy of a socially responsible company is a relevant part of the corporate strategy of Telekom Srbija for the purpose of establishing a balance between economic interests, social development, environment protection and the preservation of natural resources. The Company's employees and management believe that it is the duty of all, particularly major business entities, not only to make their contribution to the society, but also responsibly, conscientiously and wisely to use the resources, invest in sustainable development and thus repay their debt to society and the community. In accordance therewith, Telekom Srbija, as an active and responsible member of society, observes the law and ethical principles generally accepted in conducting business operations and discards and deplors an illegal and unbecoming behaviour for achieving business goals which it pursues exclusively with the quality of its products and services. When the external public is in question, Telekom Srbija keeps the market, suppliers and the public informed about the operations of the Company, observing fair competition because it believes this to be in its own interest and in the interest of its customers and capital owners.

Telekom Srbija takes measures for the protection of the environment adopting environmentally-oriented technologies and methods with the aim of reducing negative impacts on the environment. In pursuing its activity, the Company takes care about such aspects of environmental protection as rational energy consumption, the prevention of waste generation, and proper waste disposal and recycling.

By investing and applying state-of-the-art telecommunications technology, the Company contributes to the application of clean technologies and technologies consuming less energy as compared to those used over the past decades.

As a company with the greatest telecommunications market share, Telekom Srbija is most certainly a major sponsor in the region and its philanthropic activities are deeply incorporated in its corporate strategic plan, thus constituting its integral part, rather than its optional activity. For this reason, corporate philanthropy represents one of the pillars of the Company and its socially responsible operations a way to contribute to sustainable development, not through individuals, but through projects intended for a large number of customers, through infrastructure which becomes a common asset and so on, through the entire society. The Company contributes to the development of true social values, offering assistance to the broader social community. Special emphasis is laid on the development of creative, talented and young people who are to become leaders in both the local and broader communities in the near future. The Company invests in projected urban and rural development, takes part in the construction of health care wards, service capacities and other forms of infrastructure and supports sustainable development in order to improve the quality of citizen's life and increase the number of donation beneficiaries.

Telekom Srbija generates various types of waste which is disposed of regularly and in accordance with legal regulations. The Company has concluded contracts on the purchase of perilous and non-perilous waste with the companies authorized for this type of activity, whereas radioactive waste is regularly handed over to the *JP Nuklearni objekti of Serbia* (PE of Nuclear Facilities of Serbia), which is the only company permitted to take over this type of waste.

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Noise emitted in the environment mainly originates from the chillers of air-conditioners installed within the Company's facilities. If there is reasonable doubt that noise levels emitted in the environment are higher than prescribed by the law, measurements are made. In the course of 2013, we did not exceed the permitted noise levels.

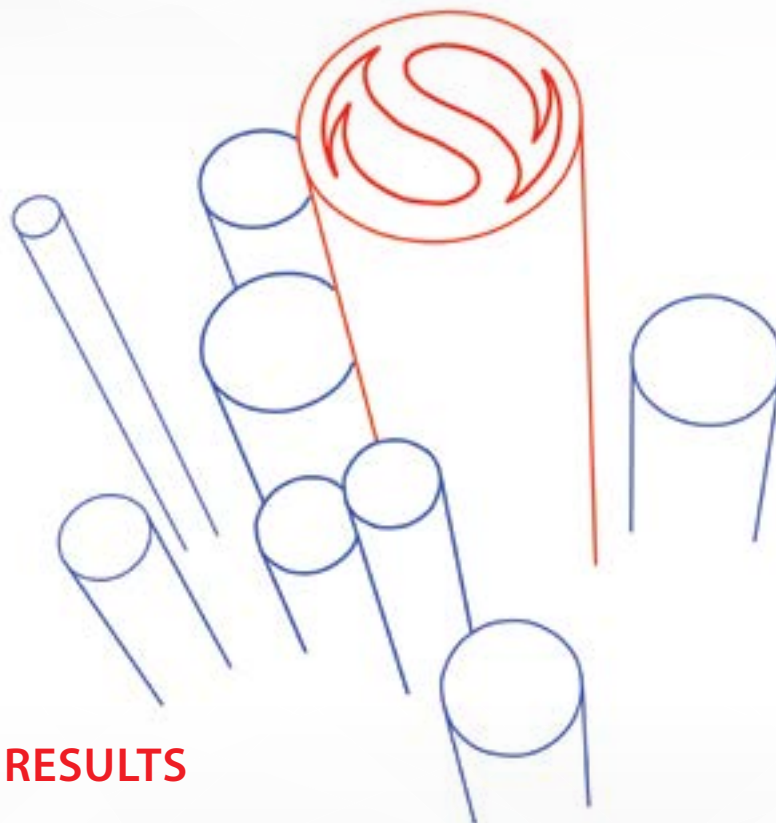
Electromagnetic radiation in the environment mainly originates from mobile radio base stations. Before the installation of a base station, a study of its effects on the environment is made listing all technical data and protection measures for that base station. Once the Study is complete, the base station is put into operation. There are regulations and standards regulating the permitted radiation levels. Before putting a radio base station into operation, the level of radiation is measured, and if third parties complain about the level of radiation, an institution is engaged to measure its levels. In accordance with the Law on Non-ionizing Radiation Protection, the measurement of the level of electromagnetic radiation by radio base stations is made every two years. So far, the radiation levels have not been exceeded.

The supply of 3,000 boxes for the disposal of waste office paper has been contracted and currently under way is the mounting of such boxes inside buildings housing offices. In this manner, the Company will collect waste paper which will not end up as communal waste.

With a string of activities of conscientious disposal of electronic waste and their responsible attitude towards nature, Telekom Srbija and its subsidiaries demonstrate their commitment to the protection of the environment and preparedness to operate in an environmentally-friendly fashion. When reaching strategic decisions, the Company takes into consideration the provisions of the applicable law regulating the environmental sphere and all potential risks of its operation and influences on the environment, particularly taking

account of the specificities of the operation of the telecommunications industry. Maintained are programmes in the sphere of energy efficiency, economic utilization of resources and electronic waste management and the activities in the sphere of waste recycling and disposal within the Company have had positive results.

FINANCIAL RESULTS



FINANCIAL RESULTS

Telekom Srbija

Income statement

In million RSD	2012	2013
Operating revenues	90.947	89.049
Operating expenditures	(75.071)	(73.870)
EBIT	15.876	15.179
EBIT margin	17,5%	17,0%
EBITDA	32.678	31.575
EBITDA margin	35,9%	35,5%
Financial revenues / (expenditures) net	(5.465)	2.037
Profit tax	841	(1.887)
Net profit	11.251	15.329
Net profit rate	12,4%	17,2%
Earnings per share	14,06	19,16

The Parent Company's income, after taxation, amounts to 15.3 billion dinars, which is an increase of 36.2% as compared to 2012. In 2013, EBIT amounts to 15.2 billion dinars, and EBITDA 3.6 billion dinars.

The net result in 2013 is significantly influenced by the positive financial sub-balance as an outcome of a reduction in foreign exchange losses and lower interest expenditure due to a significant decrease in credit liabilities, and by the revenues from dividends.

Operating revenues in the period observed amount to 89 billion dinars and are by 2.1% lower as compared to 2012, mostly due to a fall in the revenues from the traditional fixed telephony services.

Balance Sheet

In million RSD	31.12. 2012.	31.12. 2013.
NON-CURRENT ASSETS	167.845	161.990
Intangible assets	6.303	5.568
Real estate, equipment and advances	96.010	90.972
Share in the capital of subsidiaries	60.909	60.703
Other	4.623	4.747
REVOLVING ASSETS	34.565	25.935
Stocks	5.829	6.663
Receivables	13.167	13.522
Cash and cash equivalents	10.862	2.012
Other	4.707	3.738
TOTAL ASSETS	202.410	187.925
CURRENT LIABILITIES	51.458	52.355
Current account payables of long-term loans	29.931	29.870
Liabilities from business activities	6.908	8.412
Other short-term liabilities	14.619	14.073
LONG-TERM LIABILITIES	50.946	27.807
Long-term loans	46.658	23.845
Other long-term liabilities	4.288	3.962
CAPITAL	100.006	107.763
TOTAL LIABILITIES	202.410	187.925

Cash Flows

In million RSD	2012	2013
Profit before taxation	10.411	17.216
Reconciliation of profit	12.664	13.119
Net cash-in from business activities	23.075	30.335
Net cash-out from investment activities	(7.377)	(8.290)
Net cash-out from finance activities	(18.853)	(30.895)
Net cash-out of cash and cash equivalents	(3.156)	(8.850)
Cash and cash equivalents at the beginning of the year	14.019	10.862
Cash and cash equivalent at the end of the year	10.862	2.012

Ratio analysis

In million RSD	2012	2013
Total debt	76.589	53.715
Net debt	65.727	51.702
Net debt / EBITDA	2,01	1,64
Total liabilities / EBITDA	3,13	2,54
Debt ratio	39,7%	32,4%
Quick ration	0,65	0,68

A decrease in the debt to equity ratio as at 31 December 2013 is mostly due to the repayment of long-term credit liabilities.

