Hit Group Annual Report 2010

hit universe of fun


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1 STATEMENT BY THE MANAGEMENT BOARD PRESIDENT

Successfully restructuring the business and awaiting new profits

For Hit, 2010 was an exceptionally demanding year. It was the first of three years of a carefully thought-out and designed business restructuring. This was required by the very dangerous situation in which Hit found itself due to many reasons, both internal and external. Should Hit go under, it would drag down numerous employees as well as business partners, thus hitting hard the entire region. The management therefore spent the first half of 2010 identifying the main and urgent objectives, and deciding a realistic schedule to achieve them. The new road avoids completely the temptations typical of transitional countries, and we started along it aware of challenges and dangers but armed with optimism and knowledge. We prepared a strategy for 2010-2012, which, together with a corresponding action plan, represents the basis of Hit Group's stabilisation and restructuring.

As mentioned, 2010 was the first year of business stabilisation and restructuring. The feelings may be mixed, but the results achieved by both Hit and its Group are facts that support our belief that this step was both possible and sensible, as well as our determination to work seriously, professionally, responsibly and above all with a feeling for people. That is for our employees, business partners and all others who share our lives and the destiny of our company and its Group.

The results achieved by Hit in 2010 prove that we managed to turn the business around, mainly by gradually reversing the downward trend in revenues and by cutting losses by more than two thirds. Despite the large direct and indirect damage caused by a series of strikes in 2010, we managed to decrease indebtedness of the parent company, revamp the core and support business processes, reorganise operations and reduce the number of employees. More than 300 of them left the company by themselves, the majority of them with a severance. We reduced costs and expenses by almost one fourth, while still completing certain capital investments that are already earning revenues (a new poker room, several new gaming devices and games, a new customer management application). We disposed of certain financial assets and real property, and managed to ensure liquidity throughout the year.

In 2011, the second year of business restructuring, further work awaits us. If present trends continue without large disruptions, we can expect a small profit already at the end of 2011 and not only a year later as initially planned. This will finally allow us to do business as usual, and to focus on corporate climate, service quality and know-how, for which we are respected in professional circles worldwide. Of course there will also be certain capital investments, as well as new market development, also in far away places, where we will make good use of our expertise.

Not all dangers are past and gone yet: in particular there is the indebtedness of our subsidiaries. Some of them, however, were successful in reducing their losses, which resulted in an almost halved consolidated loss. Overall, we are making our business normalisation, stabilisation and restructuring scenario come true, which means that we are keeping the promise given to our employees and owners, as well as to the community.

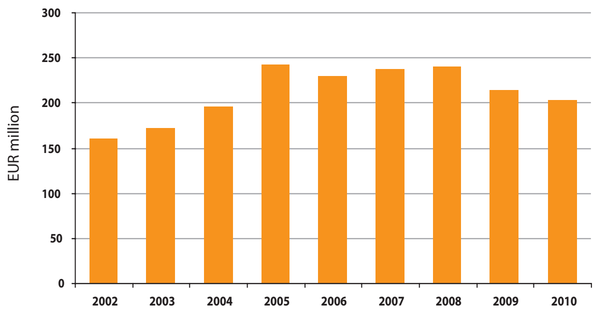
We remain committed and consistent while careful. We also remain optimists, for which we have more and more reasons.

Dr. Drago Podobnik,
Management Board President

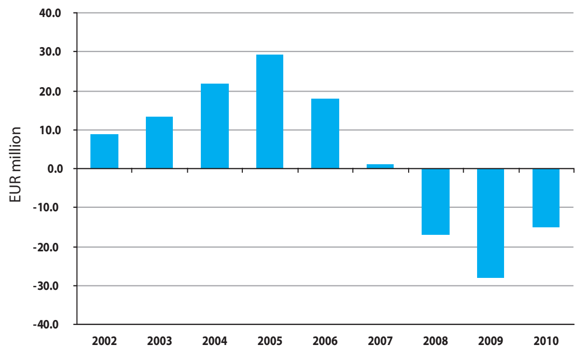
Hit Group in 2010

- EUR 230.3 million in gross operating revenues including gaming tax
- EUR 202.3 million in gross operating revenues
- EUR 15.1 million in net losses of the Hit Group
- EUR 11.8 million in net losses of the majority owner
- EUR 188.6 million in gross gaming revenues and casino entrance fees (including gaming tax and output VAT respectively)
- 2.0 million casino visits
- 477.6 thousand overnight stays
- 2,537 employees at year-end 2010
- a negative10.3-percent return on capital

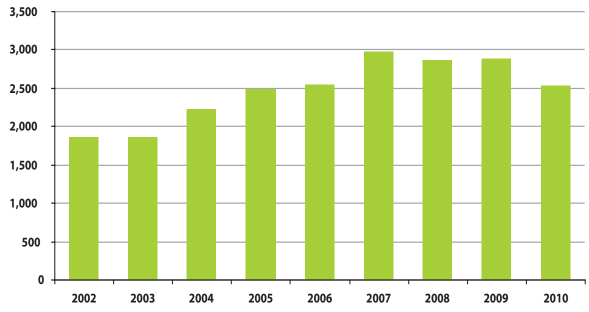
Gross operating revenues



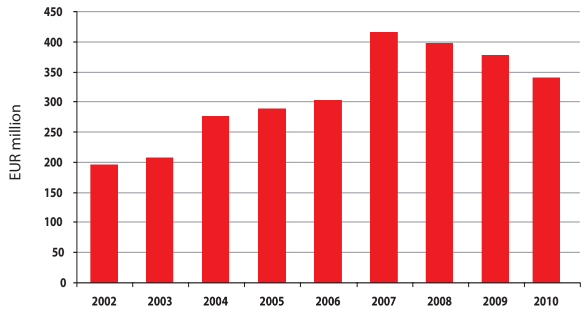
Net profit



Employees as at 31 December



Total assets as at 31 December

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1.1 Hit company profile

1.1.1 Establishment

Establishment of Hit was recorded in the register kept by the Nova Gorica District Court under no. 1/00224/00 on 9 October 1990.

The limited liability company (d.o.o.) later underwent an ownership transformation and became a company limited by shares (d.d.). Transformation was entered into the Nova Gorica District Court register pursuant to decision Srg 98/00076 on 9 February 1998.

The transformation was carried out in accordance with the Ownership Transformation of Companies with Socially-Owned Capital Organising Special Games of Chance and Capital Structure of Companies Organising Special Games of Chance Act (Official Gazette of the RS, no. 40/97, hereinafter ZLPPOD). Hit prepared an opening balance sheet as at 18 June 1994 in accordance with ZLPPOD, and determined the nominal value of its share capital at SIT 6,788,634,000 (EUR 28,328,467.70). It then issued two classes of shares as follows: 4,073,180 ordinary shares that were not freely transferable and represented 60 percent of its share capital, and 2,715,454 participating preferred shares that were freely transferable and represented 40 percent of its share capital. The nominal value of shares was SIT 1,000 (EUR 4.17).

As its shares are not listed, Hit is not obliged to comply with the Corporate Governance Code applying to companies limited by shares in the Republic of Slovenia, but nevertheless adheres to its provisions as much as possible.

Other company information as entered in the court register:

Company name: HIT hoteli, igralnice, turizem d.d. Nova Gorica
Abbreviated name: Hit d. d. Nova Gorica
Registered office: Delpinova 7a, SI - 5000 Nova Gorica
Company ID no.: 5232058
Share capital: EUR 28,328,467.70
Founders: Republic of Slovenia; entry: 2 September 1997; capital contributed: EUR 28,328,467.70

Representatives:

Dr. Drago Podobnik, Management Board President	authorisation start date: 1 August 2009
Mag. Stojan Pliberšek, Management Board Member	authorisation start date: 1 August 2009
Marjan Zahar, Management Board Member	authorisation start date: 13 June 2006
Uroš Kravos, Management Board Member	authorisation start date: 1 October 2009
Srdan Tovornik, procurator	authorisation start (end) date: 14 October 1993 (5 March 2010)

Supervisory Board composition:

Matej Golob Matzele, Chairman	mandate start (end) date: 4 July 2009 (25 August 2010)
Gorazd Podbevšek, Chairman	mandate start date: 25 August 2010
Marko Slivnik, Member	mandate start (end) date: 22 June 2006 (24 June 2010)
Marijan Stojko, Member	mandate start (end) date: 22 February 2006 (22 February 2010)
Žarko Šuligoj, Member	mandate start (end) date: 22 February 2010 (24 June 2010)
Tomislav Malnarič, Member	mandate start date: 5 March 2009
Irena Uršič, Member	mandate start (end) date: 25 March 2009 (16 September 2010)
Andrej Miška, Member	mandate start (end) date: 25 March 2009 (03 May 2011)
Karlo Korče, Member	mandate start date: 24 June 2010
Aleksander Lisjak, Member	mandate start (end) date: 24 June 2010 (20 December 2010)
Sergej Čujec, Member	mandate start date: 21 December 2010
Andrej Cetinski, Member	mandate start date: 3 May 2011
Marino Furlan, Member	mandate start date: 3 May 2011

The financial statements for the year ended 31 December 2010 were audited by the company BDO Revizija of Ljubljana, which expressed an unqualified opinion on these statements on 18 April 2011.

1.1.2 Share capital and ownership structure

Share capital of Hit (SIT 6,788,634,000) was determined based on the opening balance sheet as at 18 June 1994, as explained above. Following the changeover to the euro, share capital in an amount of EUR 28,328,467.70 was entered in the court register on 6 March 2007. It is divided into 6,788,634 no-par shares, of which:

- 4,073,180 (60 percent) are ordinary registered shares of no par value that are not freely transferable, and
- 2,715,454 (40 percent) are participating preferred shares of no par value that are non-voting and are freely transferable.

Compared to year-end 2009, the ownership structure did not change.
All shares are fully paid up.

Ordinary shares confer the following rights:

- the right to participate in company management,
- the right to participate in company profits,
- the right to participate in company assets remaining after its liquidation or bankruptcy.

Ordinary shares are transferable subject to prior consent of the Ministry of Finance in accordance with Article 56 of the Gaming Act (official consolidated text 1 published in the Official Gazette of the RS, no. 134/03). Transfers take effect only upon entry into the share register of Hit kept by the Central Securities Clearing Corporation in accordance with regulations governing dematerialised securities.

Participating preferred shares do not confer the right to company management. Their owners have the right to participate in company profits (based on a resolution adopted by the general meeting of shareholders) and company assets remaining after its liquidation or bankruptcy, as well as the right to a dividend fixed at 1 percent of company book value per share. Preferred shares are freely transferable.

Hit's ownership structure

	31 December 2010		31 December 2009	
Shareholder	Shares (number)	Equity stake (percent)	Shares (number)	Equity stake (percent)
Slovenska odškodninska družba, d. d.	1,357,727	20.00	1,357,727	20.00
Kapitalska družba, d. d.	1,357,727	20.00	1,357,727	20.00
Nova Gorica municipality	1,022,614	15.06	1,022,614	15.06
Šempeter-Vrtojba municipality	183,726	2.71	183,726	2.71
Kranjska Gora municipality	131,699	1.94	131,699	1.94
Rogaška Slatina municipality	11,541	0.17	11,541	0.17
Novo mesto municipality	8,146	0.12	8,146	0.12
Total ordinary shares	**4,073,180**	**60.00**	**4,073,180**	**60.00**
Various legal persons	2,715,454	40.00	2,715,454	40.00
Total preferred shares	**2,715,454**	**40.00**	**2,715,454**	**40.00**
Total shares	**6,788,634**	**100.00**	**6,788,634**	**100.00**

1.1.3 Governance bodies

The governance bodies of Hit are its management and supervisory boards, and the general meeting of shareholders. The management board, which runs the company, is composed of the president and three members, one of whom is the employee representative. Excepting the last one, all members and the president are appointed and recalled by the supervisory board.

The supervisory board is composed of six members: two of them are employee representatives elected by the workers' council, one of them is appointed by the Government, while the remaining three are elected by the general meeting of shareholders. At year-end 2010, Gorazd Podbevšek was the Chairman of the Supervisory Board.

1.1.4 Main activities, concessions and concession duties

Hit's main activities are the following:

- organisation of special games of chance
- hotels
- restaurants and inns
- snack bars, sweet shops, coffee houses, canteens, bars
- activities of travel agents and tour operators, tourist assistance nec
- organisation of exhibitions, fairs and congresses
- operation of sports arenas and stadiums
- other recreational activities nec

In accordance with the Gaming Act (official consolidated text 1 published in the Official Gazette of the RS, no. 134/03), games of chance may only be organised on the basis of a concession or licence granted by the competent body. Hit obtained five concessions for organising special games of chance in casinos, and concluded relevant concession contracts for the period from 1 July 1999 to 30 June 2004. On 24 June 2004, the Government adopted a resolution on their extension until 30 June 2009. On 24 June 2009, the Government adopted another resolution on extension until 30 June 2014 of the concessions granted for the following casinos:

- Casino Park, Nova Gorica,
- Casino Perla, Nova Gorica,
- Casino Korona, Kranjska Gora, and
- Casino Fontana, Rogaška Slatina.

Hit was also granted a concession for organising special games of chance in slots halls, namely for its Casinò Drive-in (Vrtojba). The concession expires on 5 December 2015.

Hit as concessionaire must calculate and pay the concession duty as laid down in the Gaming Tax Act (Official Gazette of the RS, no. 57/99) and the Gaming Act, separately for each concession granted. The basis for calculation is the amount paid in by players to participate at a certain special game of chance, as reduced by the winnings paid out to the players and revenues earned by the gaming establishment in the case of games played by players against each other. In the period 2004-2010, Hit accounted for and paid the concession duty at a rate of 5 percent, except for slot machines, in which case a progressive scale applied for casinos and a fixed rate of 20 percent applied for slots halls.

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2 BUSINESS REPORT

2.1 Introduction

At year-end 2010, the Hit Group comprised the parent Hit company and nine subsidiaries. Five were established in Slovenia and three (plus one about to be established) in the area of the former Yugoslavia. In 2010, Hit Coloseum of Sarajevo, Bosnia and Herzegovina, became 100-percent owned by Hit, while a bankruptcy procedure against another subsidiary, ICIT, commenced in May 2010.

For the parent **Hit company**, 2010 was a difficult but still successful year, the first in the three-year business restructuring period. Throughout the year, Hit implemented numerous measures provided for in the restructuring action plan as well as in the 2010 business plan, trying to reverse the downward performance trends. The revenue-increasing measures eventually helped reverse the downward trend in revenues, while the cost-optimising measures helped reduce costs. The resulting positive performance indicators could have been even better had there not be certain adverse events, such as the series of strikes organised by the gaming trade union, as well as gaming law amendments affecting tip distribution and increasing competition, to mention but a few. This mainly reflected negatively on lost revenues and higher labour costs. The latter also increased due to large severance payments, as the company was left by more employees than anticipated. However, these were one-off costs and only affected the 2010 results. These were, as with the 2009 results, affected also by the impairment of assets.

Hit Montenegro of Budva, Montenegro was successful in 2010. Its profits, as well as other performance indicators, confirm its position as one of the best companies in the Hit Group and also in Montenegro. Given the circumstances in the hotel and gaming market, which was hit badly by a decline in demand and the negative effects of the global economic crisis, the results are even better than they seem. In 2010, the company completed the expansion of the Maestral Hotel, thus obtaining additional hotel rooms, a new reception hall and a revamped exterior. It now has one of the most diverse tourist resorts on the South Adriatic Coast, which represents a sound basis for its operations in the longer term.

Hit Coloseum of Sarajevo, Bosnia and Herzegovina managed to earn a profit in 2010 which exceeded the 2010 target figure and the 2009 figure. In 2010, the company mainly focused on consolidating its position in the gaming market, and managed in increasing the number of foreign casino visitors, which offset the fall in the number of local casino visitors. However, the company also felt the adverse affect of the so-called Brčko suit, which paralysed its capital investments and could eventually endanger its market position. Nevertheless, the company enjoys the reputation of a serious, professional and reliable partner in Bosnia and Herzegovina.

Casino Kristal Umag of Umag, Croatia did not achieve the 2010 target figures, but nevertheless improved slightly the 2009 figures. The main reason for its underachievement was the drop in visitor spending, reflecting the recession and the abounding competition in the gaming market. The company made a loss in 2010 and further increased the excess of loss over equity, as well as the excess of short-term and long-term liabilities over its total assets, which threatens its future.

Casino Kobarid of Most na Soči, Slovenia did not achieve the 2010 target figures, but nevertheless improved the 2009 figures. The main reason for its underachievement is the persisting difficult business environment, while the improvement compared to 2009 is attributable to several marketing activities and a cost reduction programme. In May 2010, when it obtained a licence for organising online special games of chance, the company launched an online casino supported by a marketing campaign.

Hit Šentilj of Šentilj v Slovenskih goricah, Slovenia did better in 2010. Compared to 2009, it increased the number of visits and gross gaming revenues and at the same time reduced costs, thus reducing the loss from operations. This is attributable to its innovative marketing approach, its enhanced presence in the key market, its aggressive advertising and its richer product, but also to a shift in business attitude.

Hit Larix of Kranjska Gora, Slovenia posted a net profit also in 2010. This was slightly below the 2009 figure, mainly due to a fall in customers' purchasing power, as well as a six-month partial and one-month full closure of the main road from Austria, the company's main market. Adopting an aggressive marketing approach and modernising its slot machines, the company tried to neutralise these negative effect. In 2010, its contract on concession for organising special games of chance in casinos was extended for another five years.

Hit Alpinea of Kranjska Gora, Slovenia reduced its loss compared to 2009, despite the difficult business conditions. It adopted various measures aimed at increasing revenues and reducing costs, and adjusted its sales policy. The loss posted in 2010 is mainly the result of the customers' habits changed by the economic crisis, as well as employee, organisational, financial and technical difficulties. Management prepared a financial restructuring plan for the period 2010-2013, and adopted other measures to ensure, together with the owners, stable conditions for operations in the long term.

Hit Bovec of Bovec, Slovenia also did better than in 2009, but still fell short of the 2010 target figures. This is mainly explainable by the tightened economic conditions, bad summer weather, late start of the skiing season, and termination of the contract for the lease of the Prestreljenik restaurant.

Hit International of Belgrade, Serbia was mainly dormant in 2010. This was due to the fact that the local government unilaterally changed the concession contract awarded to the company, worsening its position compared to other local concessionaires. At year-end 2009, the company therefore decided to try and reach an agreement with the local government to lift the territorial restriction imposed. However, the agreement was not reached and the government, again unilaterally, terminated the concession contract by reason of the company's failure to meet obligations.

A bankruptcy procedure commenced against **ICIT** of Šempeter pri Gorici, Slovenia on 6 May 2010. Since August 2009, the company had liquidity problems brought about by the financial and economic crisis. This hit the company's customers to such extent that they became unable to pay their liabilities in a timely fashion.

In 2010, the **Hit Group** generated EUR 208.1 million of revenues and incurred EUR 225.1 million of expenses, thus producing a net loss of EUR 15.1 million. At year-end 2010, its assets amounted to EUR 343.2 million, and were financed by its own sources (capital and long-term provisions) in the amount of EUR 136.8 million.

At year-end 2010, the Hit Group employed 2,537 persons, down by 12 percent compared to a year ago.

Altogether, the Hit Group casinos and slots halls had 1,970,000 visits or 6 percent less than in 2009. Less visits than in 2009 saw the casinos pertaining to the Hit company, but also Aurora (Kobarid), Larix (Kranjska Gora), Maestral (Montenegro) and Coloseum Club (Sarajevo). The main reason for this was the much reduced spending by casino visitors related to their low purchasing power and uncertain future brought about by the general economic crisis, but also varied competition in their vicinity. The Hit Group hotels recorded 477.6 thousand overnight stays or almost 11 percent more than in 2009. The increase is mainly attributable to the new Kristal Hotel in Umag, and Hit Alpinea operating at full hotel capacities after completing the renovation of the Špik Hotel in mid-2009. At year-end 2010, visitors to casinos or slots halls had the choice of 219 gaming tables (four more than a year ago) and 4,028 slot machines (five more), while hotel guests had at their disposal 1,528 rooms (115 more) or 2,996 hotel beds (227 more).

2.2 Games of chance

2.2.1 Gross gaming revenues

Gross revenues from games of chance and casino entrance fees (including gaming tax and output VAT respectively) amounted to EUR 188.6 million in 2010, down 7 percent from 2009. The decrease is mainly attributable to the casinos belonging to the Hit company affected by the further fall in the number of visits brought about by the economic crisis, the series of announced and effected strikes of gaming employees, the shorter working hours and the reduced number of gaming tables since September 2010 in Casino Park, as well as the increased competition. Other Group casinos (Maestral, Coloseum Club and Larix) also saw their gross gaming revenues decrease, mainly due to the difficult business conditions created by the crisis and the ever stronger competitors.

The casinos and slots halls pertaining to the Hit company still accounted for as much as 74.8 percent (EUR 141.1 million) of gross gaming revenues earned by the Group. The subsidiaries established in Slovenia earned 12.5 percent (EUR 23.6 million), while those established abroad earned 12.7 percent (EUR 23.9 million).

Gross gaming revenues from **gaming tables** were EUR 64.1 million, down 9 percent from 2009, while those from **slot machines** were EUR 124.2 million, down 5 percent from 2009. **Other gross gaming revenues** (from bingo and sports betting) and **casino entrance fees** were EUR 0.3 million, up 31 percent from 2009. Slot machines contributed the most to total gross gaming revenues and casino entrance fees (65.9 percent), followed by gaming tables (34.0 percent) and other games and entrance fees (less than 0.2 percent). The **structure of gross gaming revenues and casino entrance fees** changed, as the contribution from slot machines increased by 0.9 percentage points compared to 2009.

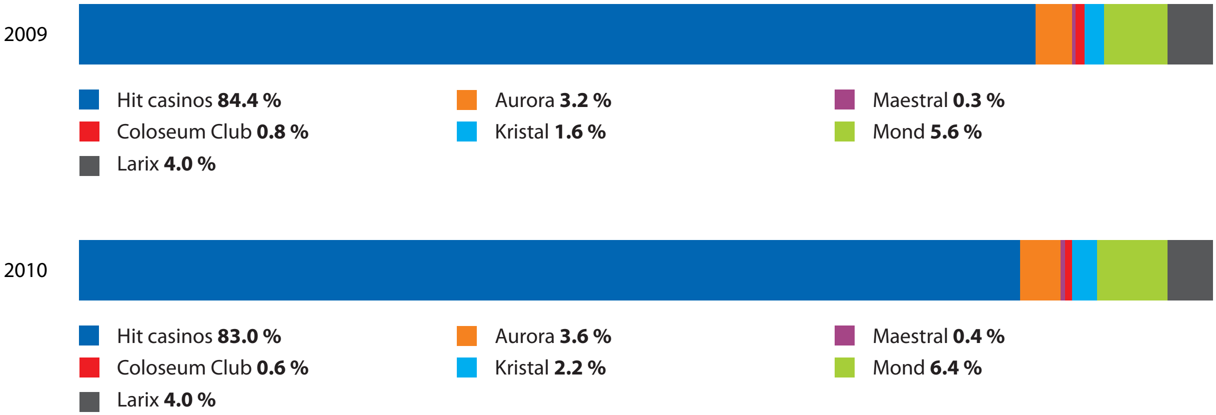
Gross gaming revenues by gaming establishment (million EUR)

	2010	Share	2009	Index 10/09
Hit casinos	141.1	74.8 %	153.9	92
Aurora	6.3	3.3 %	6.2	101
Maestral	12.5	6.6 %	14.1	89
Coloseum Club	3.8	2.0 %	3.8	99
Kristal	7.6	4.0 %	6.4	119
Mond	11.9	6.3 %	11.5	103
Larix	5.4	2.9 %	5.8	93
Total	**188.6**	**100.0 %**	**201.7**	**93**

2.2.2 Gaming tax and other duties

In 2010, all Hit Group casinos and slots halls paid EUR 51,7 million of **gaming tax and other duties**, which represented 27.4 percent of gross gaming revenues and casino entrance fees. **Gaming tax** was EUR 28.0 million, while **concession and other duties** were EUR 23.7 million. Compared to 2009, gaming tax and other duties fell by 7 percent, while their share of gross gaming revenues and entrance fees fell by 0.1 percentage points. Of total gaming tax and other duties, the casinos and slots halls established in Slovenia paid EUR 50.1 million or 96.9 percent.

Gaming tax and other duties by gaming establishment



Companies established in Slovenia, i.e. Hit, Casino Kobarid and Hit Šentilj, engage not only in games of chance, an activity that is exempt from VAT under the VAT Act, but also in other activities (of which the most important is F&B). They may deduct input VAT only in a percentage corresponding to the portion that VAT-liable activities contribute to total revenues. In 2010, this portion was 10 percent, 3 percent and 5 percent in Hit, Casino Kobarid and Hit Šentilj respectively, which means that the net value of each invoice they received was actually increased by the amount of non-deductible input VAT. This non-deductible input VAT represents an additional tax burden for casinos and thus entire companies, and significantly increases their operating costs.

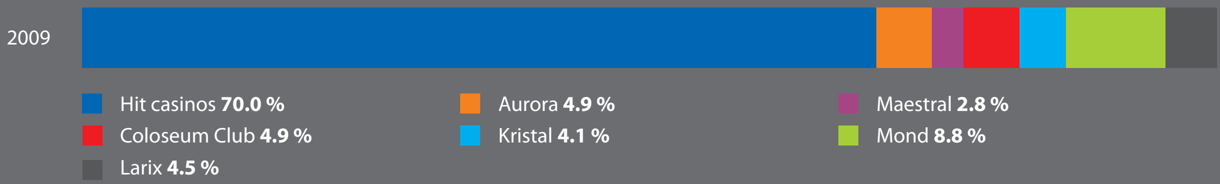
2.2.3 Visits

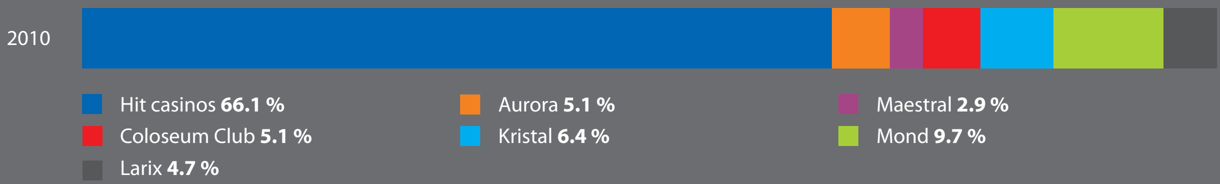
In 2010, the Hit Group casinos recorded 1,970,000 **visits**, down 125 thousand or 6 percent from 2009. The decrease is mainly attributable to the casinos and slots halls pertaining to the Hit company (down 11 percent) and to a lesser extent to the Aurora, Maestral and Coloseum Club casinos and the Larix slots hall. The decrease is explainable by the low purchasing power brought about by the economic crisis, and strong competition. Another factor with an adverse effect on the number of visits was the strikes of gaming employees announced for and effected in May and December. The Kristal and Mond casinos saw an increase in the number of visits. Casinos and slots halls located outside Slovenia accounted for 14.4 percent of the Group's total visits, up 2.6 percentage points from 2009. Visits to the casinos and slots halls established in Slovenia were 1,684,000 and accounted for 85,6 percent of the Group's total visits.

Visits by gaming establishment (thousands)

	2010	Share	2009	Index 10/09
Hit casinos	1,303	66.1 %	1,466	89
Aurora	100	5.1 %	103	98
Maestral	57	2.9 %	58	97
Coloseum Club	100	5.1 %	103	97
Kristal	85	6.4 %	85	148
Mond	185	9.7 %	185	104
Larix	92	4.7 %	95	97
Total	**1,970**	**100.0 %**	**2,095**	**94**

Visits by gaming establishment





2.3 Hotels and other tourism services

2.3.1 Revenues

In 2010, gross operating revenues from rooms sold and other tourism services provided were EUR 35.2 million, up 5 percent from 2009.

2.3.2 Available rooms and occupancy

At year-end 2010, there were 1,528 rooms within the Hit Group available to hotel guests, which is 115 more than a year ago. The number of rooms increased by 80 at the beginning of 2010 when Casino Kristal Umag leased the hotel within its complex, and by a further 35 in mid-2010 when the expansion of the Maestral Hotel in Montenegro was completed.

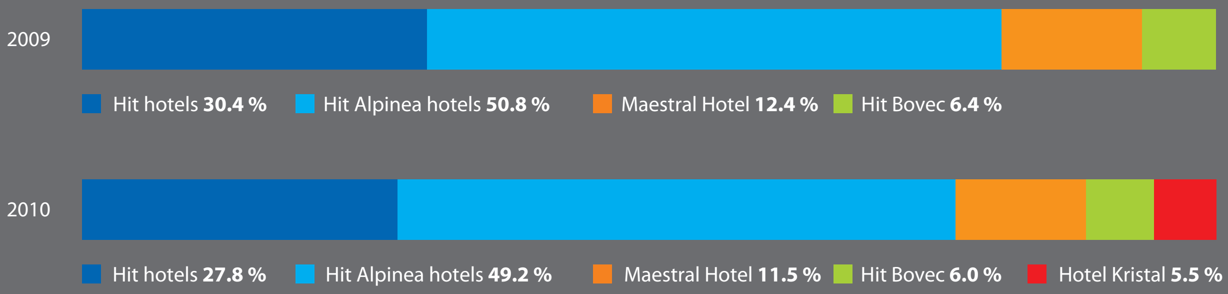
The number of overnight stays was 477.6 thousand, up 11 percent from 2009. All Hit Group companies saw an increase in the number of overnight stays. The Kristal Hotel of Umag, operating for the first year within the Hit Group, contributed the most to the overall increase, followed by the Hit Alpinea hotels that operated at full capacity throughout the year, after renovation of the Špik Hotel completed in mid-2009. Of the Group's total overnight stays, 49.2 percent was realised by the Hit Alpinea hotels, followed by the Hit hotels (slightly more than 25 percent), the Maestral Hotel (11.5 percent), the Kanin Hotel 6.0 percent) and the Kristal Hotel (5.5 percent).

In 2010, the Hit Alpinea hotels maintained the same level of occupancy as in 2009 (50 percent). The Kristal Hotel had a 47-percent occupancy, while other hotels within the Hit Group had lower occupancy rates. Some of them nevertheless increased them (Hit hotels and Kanin Hotel), while others saw theirs decrease (Maestral Hotel).

Overnight stays and bed occupancy by hotel establishment

	Overnight stays 2010			Bed occupancy	
	Number	**Share**	**Index 10/09**	**2010**	**2009**
Hit hotels	132,988	27.8 %	102	41 %	40 %
Hit Alpinea hotels	234,764	49.2 %	108	50 %	50 %
Kanin Hotel	28,582	6.0 %	104	32 %	30 %
Maestral Hotel	55,104	11.5 %	104	40 %	43 %
Kristal Hotel	26,159	5.5 %	/	47 %	/
Total	**477,597**	**100.0 %**	**111**	**/**	**/**

Overnight stays by hotel establihsment



2.4 Other activities

Other activities pursued within the Hit Group (various services, a tourist agency, wellness, etc.) earned gross operating revenues of EUR 5.6 million, down 23 percent from 2009.

2.5 Revenue breakdown

The Group's **gross operating revenues** in 2010 were EUR 202.3 million, down 5 percent from 2009. Of this amount, EUR 170.0 million or 84 percent were generated by Group companies established in Slovenia, while the remaining EUR 32.3 million or 16 percent were generated by Group companies established abroad. Gross operating revenues represented 97.2 percent of total revenues.

The share of the Group's gross operating revenues generated by games of chance (gaming tax not considered) was 79.8 percent, the share generated by hotels and other tourism activities was 17.4 percent, while the share generated by other activities was 2.8 percent. The share of hotels and other tourism activities increased by 1.7 percentage points.

Financial revenues were EUR 5.3 million or 2.5 percent of total revenues, while **other revenues** were EUR 0.6 million or 0.3 percent of total revenues.

The Group's **total revenues** (operating, financial and other) were EUR 208.1 million in 2010, down 4 percent from 2009.

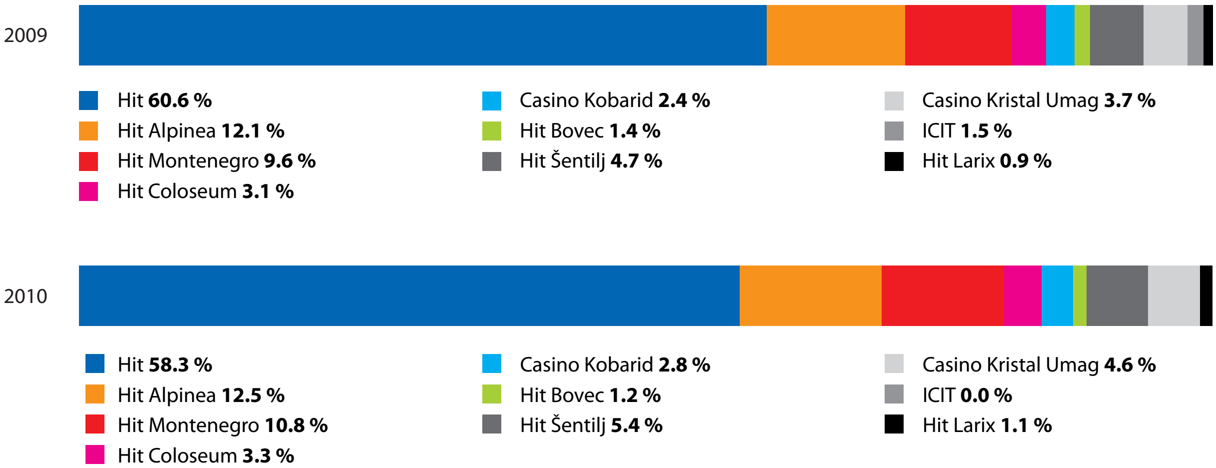
The Group's **total expenses** were EUR 225.1 million in 2010, down 10 percent from 2009.

Consolidated net loss of the Hit Group was thus EUR 15.1 million or 7.3 percent of total revenues.

2.6 Employees

At year-end 2010, the Hit Group had 2,537 employees, of which 58.3 percent were at the parent Hit company. Compared to the end of 2009, the number of employees increased by 346, or 12 percent. The decrease is mainly attributable to the parent company and is in accordance with its business restructuring and optimisation programme, which provided also for the closure of three shops in three gaming and entertainment centres of four smaller F&B units. The decrease is also attributable to the bankruptcy procedure against ICIT commenced in May 2010, the reorganisation of the Hit Alpinea company and termination of the contract for the lease of the Prestreljenik restaurant by Hit Bovec. The number of employees of other Group companies did not change much, except for Kristal Umag, which employed persons mainly in connection with the hotel under management since year-end 2010.

Employees by Hit Group company as at year-end



The Hit Group follows a recruitment and HR development policy that is in accordance with its uniform quality standards. This means that Hit as the parent company is responsible for the transfer of knowledge, experience and quality standards to its subsidiaries through its own employees. By doing so, it ensures efficiency and brand recognition.

Employees by Hit Group company as at 31 December 2010 (by the highest level of education achieved).

	Primary and vocational (I-IV)	Secondary (V)	Higher (VI)	University or higher (VII)	total
Hit	333	722	131	294	**1,480**
Hit Alpinea	194	91	16	17	**318**
Hit Montenegro	62	165	30	16	**273**
Hit Coloseum	23	58	1	1	**83**
Casino Kobarid	13	40	6	13	**72**
Hit Bovec	22	5	2	1	**30**
Hit Šentilj	22	76	18	20	**136**
Casino Kristal Umag	27	84	2	3	**116**
Hit Larix	5	18	2	4	**29**
Total Hit Group	**701**	**1,259**	**208**	**369**	**2,537**

2.7 Capital investments and development projects

In 2010, we mainly embarked on projects aimed at supplementing, refreshing and improving our gaming and tourist products. We are well aware of the fact that in order to attract as many customers as possible and be successful, we must be better than our competitors. This is particularly important now that there are many obstacles on our road associated with the changed business conditions in the last couple of years.

In 2010, the parent **Hit** company launched several projects (capital investment, development, organisational, information technology, etc.) that will help improve its performance or achieve its goals. However, not all capital investments provided for in the action plan 2010-2012 were able to be completed due to the company's economic and business situation. The most important project in the last three years was the customer relationship management project. Within this project, the company launched a loyalty club named Privilege club in its Perla and Park gaming and entertainment centres. Other projects completed in 2010 include the following: sales promotion through online presence, electronic invoicing and Poker Room (Perla). The latter was completed in August 2010 and allowed the company to revive its gaming product by offering a room dedicated exclusively to poker and various tournaments. In accordance with its strategy for 2010-2012, the company started certain activities in 2010 within the following projects: balanced scorecard, business process renovation, competency model, salary system and creative culture. A pre-study was also prepared for a project aimed at developing the Goriška destination after 2012, and several activities were organised within the project aimed at developing entertainment centres with gaming devices in Italy.

Capital investments of **Hit Montenegro** were mainly directed towards completing the expansion of the Maestral Hotel and the renovation of the reception hall.

Hit Coloseum invested in a partial renovation of the gaming floor and in the replacement of slot machines.

Casino Kristal Umag invested in new slot machines and gaming tables.

Casino Kobarid invested above all in new slot machines, game conversion, the completion of a real property construction, a surveillance system licence and certification of an online gaming system.

Hit Šentilj invested in a summer garden, game conversion, the upgrading of gaming tables software, replacement of video control equipment and new company cars.

Hit Larix invested in the modernisation of technological equipment allowing it to follow trends and thus keeping competitive advantage. The investments were mainly directed into the replacement of slot machines and other gaming devices, a surveillance system, and customer relationship management.

Hit Alpinea invested in the water system in the Alpinea Hotel, including a water reservoir.

Hit Bovec invested in a new central heating unit, which represents an important acquisition.

2.8 Environmental protection

The Hit Group companies comply with environmental regulations and the Group's social responsibility policy. In this, they follow the example of the parent Hit company.

Group companies understand their negative impact on the environment and try to minimise it by implementing appropriate technological solutions, as well as by raising employee awareness and providing relevant employee training. Environmental care and efficient energy use form an integral part of their organisational culture. In addition to what is required by legislation, Group companies have the following in place: a separate waste collection system as well as a time plan for waste collection and cleaning of utility facilities. They also check if these activities are carried out properly.

In past years, Group companies have introduced natural gas for space heating wherever possible, as well as replaced old, environmentally-unfriendly and energy inefficient heating devices using heating oil with modern ones using natural gas.

The Hit Group continuously modernises and automates its energy systems to rationalise energy and water consumption. In this, it relies on a computer application called Rasper developed in-house for energy (natural gas, heating oil, butane-propane and electricity) and water consumption monitoring. A study was prepared for Hit Larix on its air conditioning devices, based on which these were partially optimised and electricity consumed reduced for the second consecutive year.

The parent company carried out an energy audit of its largest facility, the Perla Gaming and Entertainment Centre, and is now about to increase its energy efficiency. The most profitable model so far has been cogeneration, a project financed by an external investor who builds the relevant heat and electricity generating facility and in turn receives government premiums for the electricity produced, while selling heat for heating and hot water on site. At year-end 2010, the company was negotiating the contract with the best provider and counts on the project being completed in the second half of 2011.

2.9 Balance sheet analysis and performance indicators

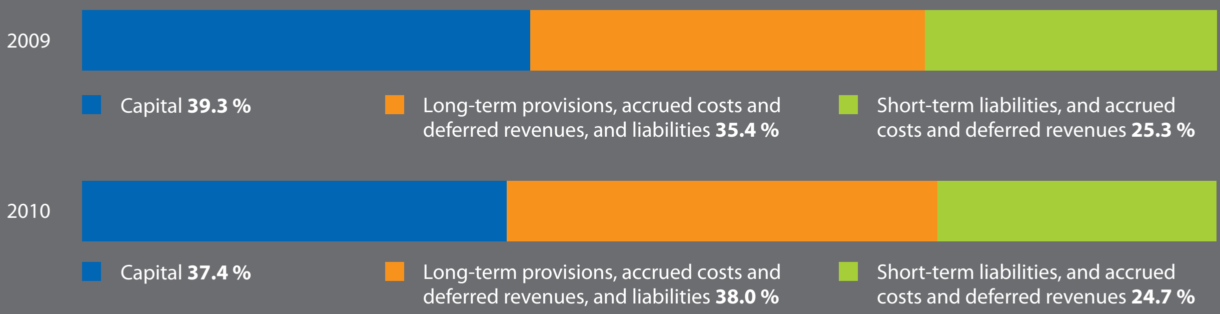
2.9.1 Capital and liabilities

At 31 December 2010, Hit Group's capital stood at EUR 128.3 million, down 14 percent from a year ago. Capital represented 37.4 percent of total capital and liabilities, which is 1.9 percentage points less than a year ago. Long-term provisions, accrued costs and deferred revenues, and liabilities decreased by 3 percent to EUR 130.2 million as at year-end 2010, when they represented 38.0 percent of total capital and liabilities (up 2.6 percentage points from 35.4 percent at year-end 2009). Short-term liabilities, and accrued costs and deferred revenues represented the remaining 24.7 percent of total capital and liabilities (EUR 84.7 million, down by 12 percent from year-end 2009). This was 0.7 percentage points less than a year ago.

Hit Group capital and liabilities as at year-end (EUR thousand)

	2010	Share	2009	Index 10/09
Capital	128,267	37.4 %	149,144	86
Long-term provisions, accrued costs and deferred revenues, and liabilities	130,243	38.0 %	134,465	97
Short-term liabilities, and accrued costs and deferred revenues	84,655	24.7 %	96,177	88
Total	**343,164**	**100.0 %**	**379,786**	**90**

Hit Group capital and liabilities as at year-end



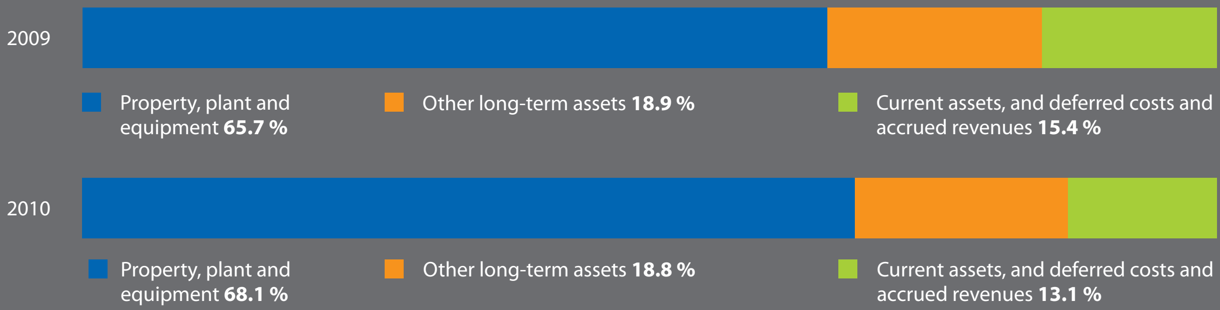
2.9.2 Assets

At year-end 2009, Hit Group's assets stood at EUR 343.2 million, down 10 percent from a year ago. Long-term assets represented as much as 86.9 percent of total assets, up 2.3 percentage points from a year ago. Short-term assets amounted to EUR 44.9 million, down 23 percent from a year ago.

Hit Group assets as at year-end (EUR thousand)

	2010	Share	2009	Index 10/09
Property, plant and equipment	233,634	68.1 %	249,644	94
Other long-term assets	64,658	18.8 %	71,802	90
Current assets, and deferred costs and accrued revenues	44,872	13.1 %	58,339	77
Total	**343,164**	**100.0 %**	**379,786**	**90**

Hit Group assets as at year-end



2.10 Performance indicators

Hit Group profitability and efficiency ratios.

	2010	2009
Return on capital	-10.3 %	-15.8 %
Return on assets	-4.2 %	-7.3 %
Revenues profitability	-7.3 %	-13.1 %
Assets turnover	0.58	0.56
Total efficiency	0.93	0.88

Return on capital, measured as the ratio of net profit/loss to average capital (excluding current year's profit/loss) was minus 10.3 percent (2009: minus 15.8 percent).

Return on assets, measured as the ratio of net profit/loss to average assets, was minus 4.2 percent (2009: minus 7.3 percent).

Revenues profitability, measured as the ratio of net profit/loss to total revenues (operating revenues plus financial revenues plus other revenues), was minus 7.3 percent (2009: minus 13.1 percent).

Assets turnover, measured as the ratio of total revenues to average assets, was 0.58 (2009: 0.56).

Total efficiency, measured as the ratio of total revenues to total costs expenses, was 0.93 (2009: 0.88).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3 MISSION AND STRATEGIC OBJECTIVES

3.1 Mission

The Hit Group mission is to satisfy the needs of its stakeholders. This is the main reason for its existence, and at the same time its guiding light and inspiration. A clear and well thought out mission gives its employees the sense that they have a common purpose, direction and opportunity.

From its very beginning the Hit Group has been inseparably connected with hotels, casinos and tourism, and has always contributed to the development of the environment where it operated. The time when merely providing services was sufficient is gone. Now the Group has to put a lot of efforts also in attracting and retaining customers, which requires careful customer relationship management. The new mission, vision and slogan all reflect this.

The Group management is aware of the importance of understanding customer needs, requirements, wishes and expectations, and of meeting these adequately while at the same time meeting also the needs of all other stakeholders. For this reason, it defined a new mission in the revised 2010-2012 Group strategy: Co-creating experiences and opportunities. With new knowledge, a professional approach and the support of all employees the Group will creatively develop the best tourist product and a broad range of accompanying services for the enjoyment, relaxation and entertainment of its customers in their free time.

3.2 Development strategy

To put its stabilisation and normalisation strategy in action, the parent Hit company defined a set of short- and medium-term measures and started implementing them. It also revised the 2010-2012 Group strategy, and defined strategic objectives and measures in view of its new values, mission and vision. They form the strategy map created based on the balanced scorecard management system, which is the main management tool.

The key strategic objectives cover four perspectives: financial, customer, business process and learning & growth. They are balanced themselves, which means that improving performance in the objectives found in one perspective may not prevent the company from improving performance in the objectives found in other perspectives. They themselves also balance short- and medium- term objectives and external and internal measures of success.

The strategy map shows connections between these strategic objectives (within the four perspectives) in the form of a cause-and-effect chain. The financial and customer perspectives contain the basic objectives of Hit, while the business process and learning & growth perspectives contain the objectives that must be achieved if Hit is to create desirable results with the first two perspectives. For each of the strategic objectives, a person responsible was appointed and strategic measures developed. For each measure, target values for the years 2010, 2011 and 2012 were defined, as well as the resources necessary for their achievement, which are set out in the strategic objective implementation programmes.

In order to earn a profit already in 2012, the parent Hit company revised the 2010-2012 strategy in December 2010 to reflect the changes in its internal and external environment.

4 BUSINESS ENVIRONMENT AND COMPETITION

4.1 Applicable regulations

Games of chance are an activity that would usually be subject to special regulation. This is the case in the majority of countries worldwide, Slovenia included. The main acts governing this area in Slovenia are the Gaming Act and the Gaming Tax Act. The gaming industry, however, is affected also by other regulations, most adversely by the Value Added Tax, as it makes investments in tourist infrastructure unattractive, which is in great contradiction with the Slovenian tourism strategy. There is also the concession duty that should be used for tourism development and promotion, which includes also infrastructure for both tourists and locals, but is not.

Rigid and strict legislation impedes development of gaming establishments. To install the latest gaming devices and software, these must undergo a very long procedure for obtaining the required permit from the State Office for Gaming Supervision, despite the fact that they have all the necessary certificates recognised by the majority of Member States (for example Italy and Austria). Manufacturers do not provide certificates especially for Slovenia, given the size of its market. Compared to their direct competitors in other Member States, the parent Hit company and its subsidiaries established in Slovenia thus have a smaller choice of gaming devices and games. In addition to all this came, in August 2007, the Restriction of the Use of Tobacco Products Act.

Development of the gaming & entertainment industry was defined in the Strategy of the Development of Gaming in Slovenia of 1997, which, however, became outdated. The Ministry of Finance and other competent institutes prepared a new one and presented it in September 2010. Hit was also involved in this process and submitted several suggestions and comments. The Government adopted the strategy in mid-December 2010. The main emphasis of the new strategy is that games of chance may be a part of Slovenia's tourism industry, and that they could benefit from regressive taxation encouraging capital investments. The new strategy is the basis for the new Gaming Act and Gaming Tax Act to be adopted by the National Assembly in 2011. All this should significantly boost Slovenia's tourism and gaming industry. New gaming legislation is being prepared also in Bosnia and Herzegovina, which will affect the subsidiary there, Hit Coloseum.

Other countries where Group companies operate have more development-oriented fiscal and other legislation. They are aware of the important role that this can play in ensuring the competitiveness of gaming establishments. Croatia, for example, exempted casinos from the anti-smoking act and thus prevented a significant drop in their revenues. In Montenegro, the local Group company was encouraged by the fiscal legislation to construct a new hotel wing in 2010.

4.2 Business environment[1]

The global economy started the year 2010 optimistically, with a surprisingly rapid recovery in the first half of the year, cooled down in the autumn and then revived at year-end. Latest estimates of the World Bank show that global GDP grew by 3.9 percent in 2010, after it fell sharply in 2008 and shrunk further in 2009. Growth accelerated the most in the industrialised countries, although the emerging economies saw twice as high GDP growth rates. Fast-growing, mainly Asian economies remained the main engine of global growth. Despite the significantly improved economic conditions in certain countries, the number of unemployed worldwide remained more or less unchanged at 205 million, which was 27.6 million more than in the pre-crisis 2007. The global unemployment rate was 6.2 percent. The global tourism industry also began to recover in 2010. Worldwide international tourist arrivals increased by almost 7 percent to a record 935 million. The pace of recovery differed, and the lowest was recorded in Europe.

In the euro area, economic activity has been strengthening since mid-2009, after a period of sharp decline. Its main drivers are exports, investments and domestic demand. Moderate economic growth was confirmed also by the fourth-quarter data, which points to a 1.7-percent euro area economic growth in 2010. Annual inflation was stable throughout 2010 at around 1.5 percent, which is slightly below the ECB's target inflation, which is below but close to 2 percent over the medium term. At year-end it jumped to 2.2 percent, for the first time after November 2008 reaching a level above 2 percent. The main drivers of inflation were rising energy prices. Unemployment rate increased to 10 percent, which translates into 15.8 million unemployed in December 2010.

The euro exchange rate strongly affected the overall euro area competitiveness. The euro depreciated against the dollar in the first half of 2010, began to strengthen in July, and then again depreciated in November and December due to the worsening fiscal problems, mainly in Ireland, Portugal, Greece and Spain. In December, one euro bought 1.3220 dollars on average.

Slovenia's economic activity strengthened in 2010, however less than the euro area average. The main driver of economic activity was foreign demand, while domestic circumstances remained uncertain, in particular those regarding financial markets and investments. Real GDP growth was 1.2 percent in 2010. Consumer price growth was 1.9 percent, moderate given the weak economic activity. Labour market conditions above all were worrying and deteriorated further at year-end. The number of registered unemployed climbed above 110 thousand, which was 13.8 percent more than in December 2009. The increase is mainly explainable with economic reasons (bankruptcies, lay-offs), as well as changes in retirement regulations. The uncertain labour market conditions resulted in modest consumer spending, despite the fact that the consumer confidence level improved by 5 percentage points compared to 2009.

Italy, Hit's most important market, has been recovering very slowly. While economic growth in the first half of 2010 was positive, it cooled down unexpectedly to zero in the fourth quarter. Annually, it was a modest 1.1 percent, mainly due to the vanishing effects of measures aimed at enhancing investment, reduced public spending and strongly increased imports. Consumer prices increased by 1.9 percent annually and were on average 1.5 percent higher than in 2009, which represents a twice as high growth as in 2009. Inflation nevertheless remained subdued. Unemployment was a pressing problem also in Italy, as it reached 8.6 percent. The number of unemployed exceeded 2.1 million. Household consumption remained accordingly modest. Overall, living standards of Italians worsened, including those of the highest income group.

Austria began recovering in mid-2009 and has been recovering at a pace higher than expected. Economic activity increased in the first half of 2010 and continued in the same manner also in the second half, as GDP is estimated to have grown by more than 2 percent annually. The main drivers were strong exports, an expansive monetary and fiscal policy in the euro area, and high growth rates in the fast-developing economies. Labour market conditions were not bad, which is mainly attributable to the growing industrial production. Unemployment level remained at a low level of around 4.5 percent, while inflation was 2.2 percent annually (on average, prices increased by 1.7 percent).

According to the national central bank, GDP shrank between 0.5 and 1.5 percent in Montenegro, less than a year ago when it shrank by 5.7 percent. Negative developments persisted in the real property market and impacted negatively on the construction sector, while trade imbalance improved. The latter is mainly explainable by the slower economic activity in the first half of 2010. Montenegro belongs to a region of moderately indebted countries where public debt is, however, following an upward trend. Risks are less pronounced in the shorter term and much more so in the medium- and longer-term, with credit risk prevailing. The average monthly rate of registered unemployment was around 12 percent, while consumer prices grew by 0.5 percent on average.

[1] *All figures in this section are the latest figures published by relevant institutions (Institute of Macroeconomic Analysis and Development of the Republic of Slovenia, national statistical offices and central banks, European Commission, IMF, World Bank, EBRD and others).*

Latest estimates show that Bosnia and Herzegovina saw a 0.9-percent increase in its real GDP. This makes it part of the group of countries who managed to get in the positive territory after the recession. A major problem currently faced by the country is the slow implementation of the economic reform programme, connected also with its internal political instability that is a drag on economic growth, foreign investment and international trade. According to the International Monetary Fund and European Commission, the country must speed up privatisation and structural reforms suspended in 2010 due to elections, and maintain economic activity and employment levels using the funds obtained from international financial institutions. Annual inflation in 2010 was 3.1 percent. At year-end, the number of unemployed was 522 thousand which accounted for a more than 40-percent registered unemployment rate.

In Croatia, the negative growth rate continued also in 2010, but at a slower pace. Personal, state and investment consumption all followed a negative trend. In 2010, Croatia is estimated to have recorded a negative 1.5 percent growth. Unemployment is supposed to be one of the factors behind this. The registered unemployment rate in December 2010 was 18.8 percent or 2.1 percentage points more than a year ago. The number of registered unemployed was 319,800 at year-end, 28,300 or 9.7 percent more than a year ago. Inflation remained low and stable due to the low domestic consumption, absent import price pressures and declining economic activity. Average inflation in 2010 was 1.1 percent, the lowest in recent Croatian history.

4.3 Competition

Competition on the western and northern state borders affected importantly the operations of the parent company and its subsidiaries established in Slovenia. The competing slots halls in the Goriška region and its surroundings improved their products and services in 2010, modernised their gaming devices and adopted an even more aggressive marketing approach. Fortuna and Venko achieved very good results, while others saw relatively huge drops in gross gaming revenues and visits. Among the latter were also the competitors operating in the Gorenjska region, Casino Bled and Casino Tivoli. In September, a new competitor, Casino Admiral, opened its doors in Kozina, directly behind Trieste.

Italian casinos managed to significantly reduce the drop in their gaming revenues and visits recorded in 2009, while one, the Saint-Vincent casino, even increased them. Among other things, they increased the number of and modernised their gaming devices, improved their service, opened smoking halls, and negotiated with the authorities to lower taxes and lift restrictions preventing local visitors from visiting the casinos. Other games of chance recorded high growth in pay-ins and consequently profits. The growth is mainly attributable to the so-called newslots (slot machines outside casinos), sports betting, lotteries (SuperEnalotto) and online poker tournaments. An important novelty were also the so-called VLT[2] slot machines, which appeared also in the nearby Veneto region. They are mainly being installed by the existing smaller slots halls with a customer base similar to that of the slots halls offering slot machines of the type "Comma 6a".

The main competitors in the Austrian market remain the casinos in Velden and Graz, which have an important advantage over the casinos established in Slovenia: they allow smoking on the gaming floor. The Graz casino nevertheless saw its gross gaming revenues drop significantly also due to the Hit's Mond casino (Šentilj). On the other hand, the Velden casino is one of the few casinos that did not have to face a drop in its gross gaming revenues after the global crisis. In June 2010, the Austrian Parliament adopted a new gaming law that will enter into force in 2014 (for slot machines) and in 2015 (for all other games of chance) respectively. The main changes that it brings about are the increased number of the so-called large licences, certain restrictions applying to the operators of slots halls and individual slot machines, the introduction of poker, and an additional gaming tax of 10 percent of gross gaming revenues. When in force, these changes are expected to give rise to a competitor to the current monopolist Casino Austria.

[2] *Video Lottery Terminals are devices similar to slot machines but linked into a centralised computer system.*

Competition to Hit Montenegro changed mainly as regards its Maestral Casino, but not also the Maestral Hotel. A new Royal casino opened in Splendid that adopted the Hit's model of flying in organised groups from Italy, as well as the Hit's concept of entertainment programme. This affected negatively revenues of Hit Montenegro in the second half of the year.

The main competitor of Hit Coloseum remains the national lottery. This expanded its product and now offers also live games in its slots hall located in the very centre of Sarajevo, thus taking away a certain percentage of customers from Coloseum Club. A new casino with Spanish owners also opened its doors in the Holiday Inn Hotel. There are also numerous slots halls and sports betting outlets in Sarajevo. One of their competitive advantages is that visitors are not required to register on entering.

The main competitors of Casino Kristal Umag were in 2010 Casino Mulino, Casino Miro and four slots clubs in Umag and its surroundings, as well as the Casino Portorož and slots halls on the other side of the border, on Slovenian coast. The main competitor is Casino Mulino that follows an individual approach to customers from its target segment, offers an entertainment programme and has a thematic interior design. The whole Istra is home to numerous slots clubs that offer, in addition to slot machines, also other games such as billiards, flippers and sports betting, which attracts mainly younger local visitors. As regards hotels, the main competition came from those belonging to the groups Sol Melia and Kempinski Adriatic.


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5 SOCIAL RESPONSIBILITY POLICY

Active social responsibility of the Hit Group

In pursuing its business objectives, the Hit Group has always endeavoured to maintain good relations with its narrow and broad social environment in the long term. Social responsibility for the Hit Group is caring for its employees, business partners and other stakeholders while being part of the social and natural environment.

Important elements of Hit's social responsibility policy are sponsorships, donations and various development projects which it supports or takes part in. In 2010, in accordance with its restructuring, the Hit Group made rational cuts to its direct funding of various social, cultural, professional, educational and sports activities, but endeavoured to support and take part in these using selected market communication tools.

The summer was rich with sports events. The parent Hit company sponsored the Vitranc Cup in Kranjska Gora, while the subsidiary Hit Alpinea sponsored the accompanying X-Plosion of Fun event. Hit also supported the best skiers, among them Ilka Štuhec, Andrej Jerman and Jure Košir, as well as hockey players (Anže Kopitar). Also in Kranjska Gora, it supported the 57th Catering and Tourism Assembly and within it a competition of professionals from these fields, in which the Hit Group employees also participated. Hit also supports the local Vitranc sports hall and women's basketball club. Hit sponsored also the Acroni hockey club of Jesenice, and the Austrian hockey clubs EC KAS Klagenfurt and VSV Villach. Hit Group has also continued its long-standing promotion of Bovec as tourist destination.

For years now the Hit Group has been implementing its social responsibility policy through various events that it organises itself or supports with its know-how. It has also developed several activities with an important social impact. Such involvement has proved to be crucial for building its reputation and trust among people, be it its own employees or others connected with its operations. When it opened a new Poker Room in August 2010 to boost the appeal and image of its Perla Gaming and Entertainment Centre, the parent Hit company for example launched several humanitarian actions. One of these was a charity poker tournament to which it invited Slovenian and Italian poker players, as well as its business partners.

Its Perla Gaming and Entertainment Centre again hosted the traditional chess tournament, the 15th in a row, and Hit also continued supporting the Solkan Kayak Centre. As always, the company feels especially responsible towards sports clubs and educational and cultural institutions. It has been a long-standing sponsor of the Young Football Player Club of Nova Gorica that has more than 400 members, but also of the Nova Gorica football club, female volleyball club and cycling club.

Hit Group is dedicated to assisting those most in need, from the youngest to the oldest. It happily assists the Sonček Association that takes care of many children's sports and social life. It also supports socially weaker families, as well as, together with the Solkan Rotary Club, individuals in need, the Stara Gora Hospital for Disable Youth, the Nova Gorica Diabetes Association and the Friends of the Youth Association. With its amortised computer and other equipment it has also helped many associations and smaller sports clubs to survive.

The Group remains closely connected with the regional cultural life. The Paviljon art gallery in its business centre launched the 13th exhibition season, which was mainly dedicated to the 25th anniversary of Hit Casinos, but also included an exhibition of painter Damjana Plešnar.

Hit's social responsibility goes beyond national borders and extends to Croatia, Montenegro and Bosnia and Herzegovina, where Group companies operate. There it supported various sports clubs and associations, innovative events and charities, helped areas hit by natural disasters, and otherwise built its relationships with local communities.

6. AUDITOR'S REPORT

6.1 Auditor’s report – consolidated financial statements

INDEPENDENT AUDITOR'S REPORT
(translation from Slovenian)

To the shareholders of the company:
HIT d.d., Delpinova 7a, Nova Gorica

We audited the accompanying consolidated financial statements of HIT d.d., which comprise consolidated balance sheet as at 31 December 2010, consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, as well as a summary of significant accounting policies and other explanatory notes. We also audited the business report.

Management’s responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements prepared in accordance with Slovenian Accounting Standards, and such internal controls as deemed necessary to enable the preparation of financial statements that are free of material misstatements, whether due to fraud or error.

Auditor’s responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free of material misstatements.
An audit involves procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgement, including the assessment of the risks of misstatements in the financial statements, whether due to fraud or error. In making those risks assessments, we consider internal control relevant to the entity’s preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
We believe that the audit evidence we obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the financial position of the company HIT d.d. as at 31 December 2010, as well as of the results of its operations and cash flows for the year then ended in accordance with Slovenian Accounting Standards.

Emphasis of matter

We draw attention to Note 14.1.50 (Off-balance sheet liabilities) to the consolidated financial statements, which describes the exposure of the Hit Group for the guarantees given to other legal persons for which it did not create provisions in its financial statements and which represent contingent liabilities. Our opinion is not qualified in respect of this matter.

Other matters

In our opinion, the business report is consistent with the audited consolidated financial statements.

Ljubljana, 17 May 2011

IBDO REvizija d.o.o.
Mag. Nadja Knez
Certified Auditor
Director (signature and seal)

7. CONSOLIDATED FINANCIAL STATEMENTS

7.1 Consolidated income statement

	2010 (EUR)	2009 (EUR)
Net sales revenues	196.516.863	210.310.120
Change in inventories of products and work in progress	93.741	(366.072)
Capitalised own products and services	1.505.646	1.680.362
Revaluation and other operating revenues	4.167.268	1.844.960
Gross operating revenues	**202.283.518**	**213.469.370**
Operating expenses	**(215.221.571)**	**(232.910.106)**
Cost of goods, materials and services	(69.417.333)	(77.525.379)
Cost of goods sold and materials used	(20.336.252)	(23.181.248)
Cost of services	(49.081.081)	(54.344.131)
Labour costs	(81.167.372)	(81.436.363)
Wages and salaries	(56.732.324)	(59.532.154)
Social insurance costs	(11.020.867)	(13.369.412)
• Pension insurance costs	(6.672.971)	(9.059.393)
• Other social insurance costs	(4.347.896)	(4.310.019)
Other labour costs	(13.414.181)	(8.534.797)
Write-downs in value	(34.954.376)	(38.223.926)
Depreciation and amortisation expense, and revaluation operating expenses associated with property, plant and equipment, and intangible assets	(33.281.147)	(37.288.521)
Revaluation operating expenses associated with operating current assets	(1.673.229)	(935.405)
Other operating expenses	(29.682.490)	(35.724.438)
Operating profit	**(12.938.053)**	**(19.440.736)**
Financial revenues	**5.258.596**	**2.528.836**
Financial revenues from shares and interests	4.322.056	1.631.254
Financial revenues from other investments	3.397.207	
Other financial revenues from shares and interests	924.849	1.631.254
Financial revenues from loans and operating receivables	936.540	897.582
Financial revenues from loans to and operating receivables due from associates	51.941	37.074
Financial revenues from loans to and operating receivables due from others	884.599	860.508

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▶ continued

	2010 (EUR)	2009 (EUR)
Financial expenses	**(9.415.837)**	**(16.285.536)**
Financial expenses from impairment and write-offs of investments	(2.274.478)	(4.770.640)
Revaluation financial expenses associated with investments in associates	(201.345)	(4.005.798)
Other revaluation financial expenses	(2.073.133)	(764.842)
Financial expenses for operating and financial liabilities	(7.141.359)	(11.514.896)
Financial expenses for other operating and financial liabilities to associates		(1.835.626)
Financial expenses for other operating and financial liabilities	(6.781.907)	(9.475.940)
Financial expenses for trade payables and bills payable	(359.452)	(203.330)
Other revenues	**587.155**	**272.447**
Other expenses	**(462.783)**	**(167.108)**
Pre-tax profit or loss for the period	**(16.970.922)**	**(33.092.097)**
Income tax	(432.062)	(485.500)
Deferred taxes	2.291.940	5.229.246
Net profit or loss for the period	**(15.111.044)**	**(28.348.351)**
Net profit or loss of minority shareholders	(3.284.901)	(1.074.128)
Net profit or loss of majority shareholders	(11.826.143)	(27.274.223)

7.2 Consolidated statement of comprehensive income

	2010 (EUR)	2009 (EUR)
Net profit or loss for the period	(15.111.044)	(28.348.351)
Changes in revaluation surplus from available-for-sale financial assets	(4.600.375)	(1.490.070)
Gains and losses arising from translating the financial statements of foreign operations	411.511	194.222
Total comprehensive income for the period	**(19.299.908)**	**(29.644.199)**
Total comprehensive income of minority shareholders	(3.275.166)	(1.017.532)
Total comprehensive income of majority shareholders	(16.024.742)	(28.626.667)

7.3 Consolidated balance sheet

	31 Dec 2010 (EUR)	31 Dec 2009 (EUR)
ASSETS	**343.164.333**	**379.786.044**
Long-term assets	**298.292.467**	**321.446.733**
Intangible assets, and long-term deferred costs and accrued revenues	7.898.255	9.991.971
Long-term deferred development costs		1.551.994
Long-term property rights	3.626.204	5.425.387
Consolidated goodwill	3.013.156	3.013.156
Advances for intangible assets		
Other long-term deferred costs and accrued revenues	1.258.895	1.434
Property, plant and equipment	233.634.495	249.644.443
Land and buildings	197.342.050	201.062.889
• Land	20.321.976	20.861.781
• Buildings	177.020.074	180.201.108
Other plant and equipment	34.398.447	39.254.151
Property, plant and equipment under acquisition	1.893.998	9.327.403
• Advances for property, plant and equipment	62.724	124.900
• Property, plant and equipment under construction	1.831.274	9.202.503
Investment property	13.236.851	13.465.639
Long-term investments	29.162.895	36.196.386
Long-term investments, excluding loans	28.991.934	35.374.654
Shares and interests in associates	369.981	2.377.620
Other shares and interests	26.784.398	30.805.530
Other long-term investments	1.837.555	2.191.504
Long-term loans	170.961	821.732
Long-term loans to others	170.961	821.732
Long-term operating liabilities	1.364.229	1.489.590
Long-term operating liabilities to others	1.364.229	1.489.590
Deferred tax assets	12.995.742	10.658.704
Current assets	**38.663.680**	**46.890.223**
Assets held for sale	761.060	
Inventories	1.962.182	4.216.587
Materials	1.701.105	2.505.172

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▶ continued

	31 Dec 2010 (EUR)	31 Dec 2009 (EUR)
Work in progress		412.159
Products and merchandise	246.941	1.241.046
Advances	14.136	58.210
Short-term investments	8.973.666	14.206.775
Short-term investments, excluding loans	7.280.886	12.168.116
Other short-term investments	7.280.886	12.168.116
Short-term loans	1.692.780	2.038.659
Short-term loans to associates	657.664	657.664
Short-term loans to others	1.035.116	1.380.995
Short-term operating receivables	6.111.407	9.705.988
Short-term trade receivables	2.466.966	5.116.524
Short-term operating receivables due from associates	73.657	21.717
Short-term operating receivables due from others	3.570.784	4.567.747
Cash	20.855.365	18.760.873
Deferred costs and accrued revenues	**6.208.186**	**11.449.088**
CAPITAL AND LIABILITIES	**343.164.333**	**379.786.044**
Parent-only shareholders' capital	**128.266.668**	**149.143.810**
Called-up capital	28.328.468	28.328.468
Share capital	28.328.468	28.328.468
Capital surplus	29.618.361	29.618.361
Revenue reserves	43.243.173	55.494.377
Legal reserves	5.303.159	5.303.159
Other revenue reserves	37.940.014	50.191.218
Revaluation surplus	10.669.647	15.276.412
Capital consolidation adjustment	150.809	(257.357)
Capital of minority shareholders	16.256.210	20.683.549
Provisions, and long-term accrued costs and deferred revenues	**8.540.892**	**10.281.715**
Provisions for termination benefits and similar liabilities	3.750.762	4.649.622
Other provisions	400.000	2.500.000
Long-term accrued costs and deferred revenues	4.390.130	3.132.093
Long-term liabilities	**121.701.652**	**124.183.546**
Long-term financial liabilities	118.685.949	120.772.609
Long-term financial liabilities to banks	113.172.674	112.656.804
Long-term financial liabilities to others	5.513.275	8.115.805

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▶ continued

	31 Dec 2010 (EUR)	31 Dec 2009 (EUR)
Long-term operating liabilities	423.656	23
Long-term operating liabilities to others	423.656	23
Deferred tax liabilities	**2.592.047**	**3.410.914**
Short-term liabilities	**78.820.456**	**92.130.409**
Short-term financial liabilities	**51.292.371**	**57.767.009**
Other short-term financial liabilities to associates		1.896.283
Short-term financial liabilities to banks	49.012.200	53.792.634
Other short-term financial liabilities	2.280.171	2.078.092
Short-term operating liabilities	**27.528.085**	**34.363.400**
Short-term operating liabilities from advances	1.103.091	1.167.096
Short-term operating liabilities to associates		15.857
Short-term trade payables	11.955.147	18.295.502
Other short-term operating liabilities	14.469.847	14.884.945
Accrued costs and deferred revenues	**5.834.665**	**4.046.564**
Off-balance sheet items	19.257.615	19.430.534

7.4 Consolidated cash flow statements

	2010 (EUR)	2009 (EUR)
A. CASH FLOWS FROM OPERATING ACTIVITIES		
a) Items of income statement	**24.064.430**	**13.696.600**
Operating revenue (except from revaluation) and financial revenues from operating receivables	202.284.535	211.247.831
Operating expenses excluding depreciation or amortisation (except from revaluation) and financial expenses from operating liabilities	(179.525.124)	(202.329.670)
Income taxes and other taxes not included in operating expenses	1.305.019	4.778.439
b) Changes in net operating assets in balance sheet items (including accruals and deferrals, provisions and deferred tax assets and liabilities)	**1.578.577**	**1.317.263**

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▶ continued

	2010 (EUR)	2009 (EUR)
Opening less closing operating receivables	(256.095)	(713.257)
Opening less closing deferred costs and accrued revenue	(549.291)	(793.160)
Opening less closing deferred tax assets	(2.922.719)	(4.312.271)
Opening less closing inventories	361.667	747.516
Closing less opening operating liabilities	7.383.825	(3.168.586)
Closing less opening accrued costs and deferred revenue, and provisions	(1.527.970)	10.277.336
Closing less opening deferred tax liabilities	(910.840)	(720.315)
c) Net cash from operating activities (a + b)	**25.643.007**	**15.013.863**
B. CASH FLOWS FROM INVESTING ACTIVITIES		
a) Cash receipts from investing activities	**20.991.258**	**15.133.525**
Interest and dividends received from investing activities	878.356	1.774.674
Dividends received from investing activities	2.973.975	2.530.681
Cash receipts from disposal of intangible assets	373.411	295.735
Cash receipts from disposal of property, plant and equipment	6.236.590	652.806
Cash receipts from disposal of investment property	2.398.998	653.165
Cash receipts from disposal of long-term investments	2.630.448	8.735.106
Cash receipts from disposal of short-term of investments	5.499.480	491.358
b) Cash payments from investing activities	**(24.669.054)**	**(30.176.990)**
Cash payments to acquire intangible assets	(2.592.068)	(1.383.275)
Cash payments to acquire property, plant and equipment	(11.307.244)	(21.712.106)
Cash payments to acquire investment property		(364.476)
Cash payments to acquire long-term investments	(101.714)	(6.297.133)
Cash payments to acquire short-term investments	(10.668.028)	(420.000)
c) Net cash from investing activities (a + b)	**(3.677.796)**	**(15.043.465)**
C. CASH FLOWS FROM FINANCING ACTIVITIES		
a) Cash receipts from financing activities	**159.698.093**	**169.566.079**
Cash proceeds from paid-in capital		
Cash proceeds from increase in long-term financial liabilities	18.930.121	33.345.653
Cash proceeds from increase in short-term financial liabilities	140.767.972	136.220.426

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▶ continued

	2010 (EUR)	2009 (EUR)
b) Cash payments from financing activities	**(179.572.155)**	**(173.673.047)**
Interest paid on financing activities	(6.447.049)	(6.962.252)
Cash repayments of long-term financial liabilities	(24.345.239)	747.516
Cash repayments of short-term financial liabilities	(145.751.645)	(145.289.429)
Dividends and other profit shares paid	(3.028.222)	(3.374.800)
c) Net cash from financing activities (a + b)	**(19.874.062)**	**(4.106.968)**
D. CLOSING BALANCE OF CASH	**20.855.365**	**18.760.873**
x) Net cash inflow or outflow for the period (sum total of net cash Ac, Bc and Cc)	2.091.149	(4.136.570)
Exchange rate translation effects	3.343	3.355
y) Opening balance of cash	18.760.873	22.894.088

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