

INTERIM REPORT

ON THE ACTIVITY OF BULGARTABAC-HOLDING AD FOR THE FOURTH QUARTER OF 2011

**in accordance with Art. 100o, para. 4, i.2 of Public Offering of Securities Act (POSA)
and Art.33 of Ordinance No 2**

1. Important events, which have occurred during the fourth quarter of 2011 and their impact on the results reported in the financial statements

Completion of the procedure for privatisation of Bulgartabac-Holding AD

An important event, which has occurred in the fourth quarter of 2011, is the change in the persons exercising control over Bulgartabac-Holding AD as a result of the completed procedure for privatisation of the State participation in the company's capital.

As a result of the publicly announced tender, in pursuance of a decision № 3219-II dated 18 April 2011 (promulgated in the State Gazette, issue 34 of 10 May 2011) of the Agency of Privatisation and Post Privatisation Control (APPC), a privatisation contract between APPC and BT Invest GmbH, Austria, was signed on 12 September 2011 for the privatisation of 79.83% of the capital of Bulgartabac-Holding AD, Sofia.

On 14 October 2011, APPC, in its capacity of a seller, transferred to BT Invest GmbH, Austria, 5,881,380 shares, or 79.83% of the capital of Bulgartabac-Holding AD.

The transaction was registered with Central Depository on 14 October 2011.

Holding extraordinary General Meetings of Shareholders of Bulgartabac-Holding AD and of its subsidiaries, Sofia-BT AD, Blagoevgrad-BT AD, Pleven-BT AD, and Bulgartabac-Trading EAD

During the fourth quarter of 2011, extraordinary General Meetings of Shareholders of Bulgartabac-Holding AD (01 November 2011) and of the following its subsidiaries were held: Sofia-BT AD (21 November 2011), Blagoevgrad-BT AD (23 November 2011), Pleven-Bulgartabac AD (22 November 2011), and Bulgartabac-Trading EAD (01 December 2011). The key agenda items of the above extraordinary GMS included the replacement of the members of the Boards of Directors of these companies. The new members of the Boards of Directors were duly registered with the Trade Register at the Registry Agency.

The following decisions were passed at the extraordinary GMS of Bulgartabac-Holding AD held on 01 November 2011:

- The General Meeting of Shareholders discharged Alexander Dimitrov Manolev, Georgi Serafimov Kostov, and Ivan Atanasov Bilarev as members of the Board of Directors of the company.
- The General Meeting of Shareholders elected as members of the Board of Directors of the company:
 - Alexander Jurjevich Romanov;
 - Yavor Nikolaev Draganov;
 - Angel Dimitrov Dimitrov;

- Ventsislav Zlatkov Cholakov;
- Miglena Petrova Hristova.

- The General Meeting of Shareholders set a mandate of 3 (three) years for the members of the Board of Directors.
- The General Meeting of Shareholders approved that the amount and the terms and conditions for payment of remunerations to the members of the Board of Directors of Bulgartabac-Holding AD should be determined in accordance with the principles, indicators and criteria set in the Regulation for the Order for Exercising of the rights of the State in the Commercial Companies with State Participation in the Capital adopted by Decree No 112 of the Council of Ministers of the Republic of Bulgaria dd. 23 May 2003, together with any subsequent amendments and supplementations, which would apply in this case as well.

The amount of the management guarantees of the members of the Board of Directors of Bulgartabac-Holding AD should be determined in compliance with the effective law.

- The General Meeting of Shareholders nominated and empowered Alexander Jurjevich Romanov to conclude, on behalf of the company, contracts with the members of the Board of Directors that would not be entrusted with governance.

Registration with Trade Register at the Registry Agency of the changes in the composition of the Board of Directors of Bulgartabac-Holding AD, adopted at the extraordinary GMS of the company, as also of the individuals representing the company.

At its meeting held on 01 November 2011, the newly elected Board of Directors of Bulgartabac-Holding AD took without attendance the following resolutions:

1. On the grounds of Art. 244, para. 4 of CA, the Board of Directors assigned the company's management and elected as executive members (Executive Directors) Angel Dimitrov Dimitrov and Ventsislav Zlatkov Cholakov;

2. On the grounds of Art. 235, para. 2 of CA, the Board of Directors empowered Angel Dimitrov Dimitrov and Ventsislav Zlatkov Cholakov to represent the company before third parties, always acting jointly;

3. On the grounds of Art. 244, para. 2 of CA, the Board of Directors elected Alexander Jurjevich Romanov to be the Chairman of the Board of Directors and Yavor Nikolaev Draganov to be the Vice Chairman of the Board of Directors.

The above facts and circumstances were announced to and registered in the batch of Bulgartabac-Holding AD kept by the Trade Register at the Registry Agency on 04 November 2011 under No 20111104101533.

Registration with Trade Register at the Registry Agency of the procurator of Bulgartabac-Holding AD

By a notary certified power of attorney dated 17 November 2011 of Bulgartabac-Holding AD, represented jointly by Angel Dimitrov Dimitrov and Ventsislav Zlatkov Cholakov, Executive Directors, on the grounds of Art. 21, para.1 of CA, Ivan Atanasov Bilarev were authorized to manage and represent, in his capacity of Procurator, the commercial entity of the company always jointly with either one of the Executive Directors of the company.

The above fact was announced to and registered in the batch of Bulgartabac-Holding AD kept by the Trade Register at the Registry Agency on 18 November 2011 under No 20111118184140.

Dividends

1. At the regular General Meetings of Shareholders of the subsidiaries of Bulgartabac Group held in June 2011 decisions for distribution of dividends for 2010 were taken by the following subsidiaries:

Blagoevgrad-BT AD	BGN 31 158 447.1
Sofia-BT AD	<u>BGN 7 001 259.03</u>
	BGN
Total	38 159 706.13

Out of dividends approved, the amount of BGN 32,034,897.41 will be paid to the parent company Bulgartabac-Holding AD, and the amount of BGN 6,124,808.72 will be paid to minority shareholders.

2. The exact amount of dividends to be paid by Bulgartabac-Holding AD to its shareholders as a result of the decisions passed under items 5, 6 and 16 of the agenda of the regular GMS of the company held on 23 June 2011 is as follows:

- The total amount of dividends under items 5, 6 and 16 of the agenda is BGN 52,983,360.41, incl. for the State, represented by the Ministry Economy, Energy and Tourism – BGN 42,297,527.65 and for the minority dividends – BGN 10,685,832.76.
- Gross amount of dividends per share – BGN 7.19;
- Net amount of dividends per share /less tax on dividends of 5% for the persons under Art.194, para.1 of Corporate Income Taxation Act and the persons under Art.38, para.1 of the Personal Income Taxation Act /PITA/ - BGN 6.83.

Pursuant to the Public Offering of Securities Act, the company is bound to secure payment of the dividends voted at the General Meetings within 3 months of the date the General Meeting was held.

The initial date of payment of dividends to the shareholders of Bulgartabac-Holding AD was 24 August 2011.

Dividends to shareholders – individuals and legal entities that are clients of an investment broker will be paid through the investment broker whereat they hold subaccounts, within a three-month period as of 24 August 2011. After the expiry of the above term, the method and procedure for their payment will be additionally specified by us.

Dividends to individuals and legal entities that are not clients of an investment broker will be paid at the counters of all branches and offices of UniCredit Bulbank AD as of 24 August 2011.

The terms and conditions for dividend payment are published on the website of the company at: www.bulgartabac.bg, section „For investors”, subsection „Internal information”, as well as on the websites of FSC, BSE-Sofia and X3 News.

Regular General Meeting of Shareholders held in June 2011

At the regular General Meeting of Bulgartabac-Holding AD, Sofia, held on 23 June 2011, the following resolutions were passed in accordance with the previously announced agenda:

- The General Meeting approved the Management report of the Board of Directors on the activity of the company in 2010;
- The General Meeting approved the report of the registered auditor on the results of the audit of the company's financial statements for 2010.
- The General Meeting approved the report of the Audit Committee of the company on its activity in 2010.

- The General Meeting approved the audited annual financial statements of the company for 2010.
- The General Meeting approved the proposal of the Board of Directors for distribution of the Company's profit for 2010, as follows:
 - 10% to Reserve Fund in accordance with Art. 246, para. 2, i.1 of the Commercial Act;
 - after deducting the allocations for Reserve Fund, 80% of the profit to be distributed as dividends to the shareholders on the grounds of Art. 26 of a Council of Ministers Decree /CMD/ No. 334 of 29 December 2010 for execution of the State Budget of Republic of Bulgaria for 2011;
 - on the grounds of Art. 33, para. 9 of Regulation for the Order for Exercising of the rights of the State in the Commercial Companies with State Participation in the Capital, approved by CMD No 112 of 23 May 2003 /promulgated in State Gazette issue 51 of 03 June 2003/, latest amendment SG issue 72 of 14 September 2010, effective 14 September 2010, tantiemes to be allocated to the members of the Board of Directors of the company in an amount of one average salary as received during the year;
 - the remaining amount of the 2010 profit, after the above distributions, to be transferred to Other Reserves Fund.
- The General Meeting of Shareholders took a decision for distribution of the company's retained earnings among the shareholders of Bulgartabac-Holding AD proportionately to their shares.
- The General Meeting approved the Report of the Board of Directors on the activity of Bulgartabac Group for 2010.
- The General Meeting approved the report of the registered auditor on the results of the audit of the consolidated financial statements for 2010 of Bulgartabac Group.
- The General Meeting approved the audited consolidated annual financial statements of Bulgartabac Group for 2010.
- The General Meeting approved the report of the Investors Relations Director on his activity in 2010.
- The General Meeting approved the transactions carried out under Art. 114, para. 4 of POSA, which are disclosed in detail in the substantiated report, as follows:
 - Annex 47 of 01 February 2010 to the Trademark License Agreement No 005-L of 01 January 1995 regarding royalties for sales of tobacco products in the domestic market in the amount of BGN 4 672 797.00, VAT excluded;
 - Annex 48 of 14 June 2010 to Trademark License Agreement No 005-L of 01 January 1995 regarding royalties for sales of tobacco products in the domestic market in the amount of BGN 2 302 938.00, VAT excluded;
 - Annex 2 of 19 May 2010 to the Contract No 133-II of 03 July 2000 on the trade representation remunerations upon sales under intra-Community supplies and supplies to third countries (export) of tobacco products and cut tobacco manufactured by Blagoevgrad-BT AD in the amount of BGN 4 031 102.31, VAT excluded;
 - Contract No 347 – DP of 15 November 2010 on the sale of tobaccos owned by Bulgartabac-Holding AD in the amount of BGN 2 230 000.00, VAT excluded;
 - Contract No 353 – DP of 15 November 2010 on the sale of tobaccos owned by Bulgartabac-Holding AD in the amount of BGN 470 000.00, VAT excluded.”
- The General Meeting was against the approval of decisions under item 12.

- The General Meeting exonerated from responsibility the members of the company's Board of Directors for their activity in 2010, as follows:
 - Ivan Atanasov Bilarev
 - Alexander Dimitrov Manolev
 - Georgi Serafimov Kostov
- The General Meeting appointed the specialized audit firm HLB Bulgaria OOD, Sofia, registered auditor No 017, to audit and certify the separate and consolidated financial statements for 2011 of Bulgartabac-Holding AD.
- The General Meeting determined the remuneration of the members of the Board of Directors who will not be entrusted with the company's governance shall be determined in accordance with the principles, indicators, criteria and amounts stipulated in Art.33 of the Regulation for the Order for Exercising of the rights of the State in the Commercial Companies with State Participation in the Capital, in compliance with the requirements of Art.19, para.7 of the Administration Act, effective 01 January 2009, and Art.7, para.3 of the Civil Servants Act, effective 01 January 2009.
- The General Meeting of Shareholders took a decision for payment of dividends to the shareholders of Bulgartabac-Holding AD, proportionately to their shares, on account of item "retained earnings", account 117 "Additional Reserves" of the company, in the amount of BGN 30,193,124 (thirty million one hundred ninety-three thousand one hundred and twenty-four Bulgarian leva).

2. Development of the activity in 2011

➤ Tobacco buy-up and processing

During Q'4 of 2011, the Board of Directors of Bulgartabac-Holding AD took a decision to replace Pleven-BT AD as a party to the contracts for manufacturing and purchasing with tobacco growers of groups Basma, Kaba Koulak and Burley varieties, crop 2011. The purchasing of group Burley started late in the year and 99 tons of raw tobacco were purchased by its end. The purchasing of Burley and Basma varieties commenced in the end of 2011 and by the end of the year 364 tons of raw materials were bought up.

The tobacco buy up was done by Pleven-BT AD in accordance with the purchase contracts concluded

Considering the market situation in the sector of raw tobacco, the Board of Directors of Bulgartabac-Holding AD approved the following purchase prices by classes in BGN/kg of purchased tobacco for the variety groups Basma, Kaba Koulak and Burley, crop 2011:

Class	Variety group		
	Burley	Kaba Koulak	Basma
I class	3.90 BGN/kg	4,20 BGN/kg	7.65 BGN/kg
II class	2.60 BGN/kg	3.20 BGN/kg	5,00 BGN/kg
III class	1.40 BGN/kg	1.90 BGN/kg	1.95 BGN/kg

At the beginning of the year, the buy-up of tobacco of variety groups Basma, Kaba Koulak and Burley, crop 2010, was completed and Bulgartabac-Holding AD purchased 3,830 tons of raw tobacco, out of which by the end of July 2011, on the basis of service contracts concluded with Pleven-BT AD, 3,544 tons of finished products were manufactured.

During Q'1 of 2011, Bulgartabac-Holding AD concluded a contract with Pleven-BT AD for the

sale of tobacco stems for the amount of BGN 118 thousand (VAT excluded).

During Q'3 of the year, Bulgartabac-Holding AD sold tobacco Burley strips, crop 2010, to Blagoevgrad-BT AD and Sofia-BT AD for the amount of BGN 1 259 thousand (VAT excluded), and BGN 1 717 thousand (VAT excluded), respectively.

During Q'4 of 2011, Bulgartabac-Holding AD concluded service contracts with Pleven-BT AD for the purchase of variety groups Burley and Kaba Koulak and for the purchase of variety group Basma, as well as of for the processing of Burley and variety groups Basma and Kaba Koulak . Due to the delay in the purchasing campaign for crop 2011, during the reported period there were only partial sales made under the purchase contract. No services were performed under the processing contract. The implementation of these contracts is to take place in Q'1 of 2012.

➤ Trade in tobacco

Tobacco export

Tobacco supply in 2011 was directed mainly to tobacco dealers operating in the sector, thus on the one hand allowing the maintenance and activation of export possibilities, and on the other hand reducing significantly existing trade risks. Risks related to payment of tobacco sold were cut down to the minimum and no tobacco deliveries were made under deferred payment conditions to markets and firms at risk.

In the first nine months of 2011, tobaccos were sold under contracts concluded in 2009, 2010 and 2011. Lots from crops 2008, 2009 and 2010 were included in the export structure during this period, as also some small remaining quantities from crop 2006. If compared with 2010, in 2011 there was a decrease in the total volume of tobacco sold to unrelated parties in terms of quantity and price, and respectively, a decrease in revenue from trade representation fees upon export of tobacco. The total quantity of own tobacco sold through export, intra-Community supplies and domestic sales during 2011 was 882.7 tons, or BGN 4,199.3 thousand.

The total quantity of tobacco sold by Bulgartabac Group during 2011 was 2,083 tons amounting to BGN 10,121.7 thousand.

Tobacco import

For the needs of cigarette production, the Bulgartabac Group companies import Virginia and Burley tobaccos, tobacco stems and reconstituted tobacco. The main sources for purchasing high quality large leaf Virginia and Burley tobaccos are the countries with the most developed production and international trade – Brazil, Zimbabwe, USA, Argentina, and Malawi. Tobacco stems are imported mainly from China and Argentina, and reconstituted tobacco from France due to the sufficiently good quality characteristics and good trade terms and conditions. In 2011, 12,266 tons of raw tobacco were imported for the amount of USD 62,427 thousand and EUR 2,492 thousand. The increase in the total volume of imported tobacco in terms of quantity and price has led to a higher amount of revenue from trade representation fees upon import of tobacco.

It may be concluded that despite of the severe global financial and economic crisis, in 2011 Bulgartabac-Holding AD continued to actively implement and carry out a flexible trade policy on offering and selling Bulgarian tobacco in international markets, as well as its activity on ensuring the continuous supply of imported raw tobacco needed for the cigarette production.

The operating results from the sales of tobacco (exports, Intra Community Supplies and domestic sales to unrelated parties) by Bulgartabac-Holding AD at 31 December 2011, accumulated as of the beginning of the year 2011, were as follows:

Sales of own tobacco by Bulgartabac-Holding AD	
<i>31.12.2011</i>	<i>31.12.2010</i>
882,7 tons	1 194,2 tons
BGN 4,199.3 thousand	BGN 7,827.6 thousand

Fees from trade representation paid to Bulgartabac Holding AD re: Exports, Imports, Intra Community Supplies & Acquisitions and Domestic Sales to unrelated parties (in BGN, VAT excluded)	
<i>31.12.2011</i>	<i>31.12.2010</i>
BGN 1 463 thousand	BGN 1 052 thousand

➤ **Trade in tobacco products**

Subsidiaries pay fees to Bulgartabac-Holding AD for rights over trademarks (royalties), as well as fees for trade representation for export of cigarettes made by Bulgartabac-Holding AD on their account.

Royalties for Bulgartabac-Holding AD in relation to rights of trademarks	
<i>31.12.2011</i>	<i>31.12.2010</i>
BGN 13,173 thousand	BGN 10,862 thousand

Fees for Bulgartabac-Holding AD under contracts for trade representation in export of cigarettes	
<i>31.12.2011</i>	<i>31.12.2010</i>
BGN 7,270 thousand	BGN 6,882 thousand

Domestic market of tobacco products

The policy pursued by Bulgartabac-Holding AD during 2011 is entirely consistent with the market conditions and is subject to the aim of stabilizing and maintaining the positions on the domestic market achieved in the end of 2010.

In 2011, the company maintained the volume of sales compared with that achieved in 2010, despite of the declining volumes in the banderol market.

The usual fluctuations in the separate months are observed during the reporting period; in general, however, we report a trend of regaining the company's market share.

Since the beginning of the year Bulgartabac-Holding AD has been manufacturing and marketing to the domestic market a new format of consumer pack containing 10 cigarettes by the piece of the well-known brands Melnik, MM and GD, the brand GD being one of the top in the segment of 10-cigarette packs.

In Q'3 of 2011 Bulgartabac-Holding AD commenced the production of Reduced Ignition Propensity cigarettes, or the so called "RIP cigarettes", which comply with Standard EN

16156:2010 for fire safety in accordance with the new regulation adopted within the European Union and the introduction, as of 17 November 2011, of a new standard for tobacco products manufacturing by using special cigarette paper.

The market of tobacco products during the reporting period was characterized by extraordinary dynamics and experienced a number of objective factors which had a direct impact on the sales of cigarettes on the domestic market:

- *Pricing policy and competition*

During the current calendar year, for the first time in the last five years, the excise duty rate of tobacco products was not changed and the 2010 levels were kept. Nevertheless, the declining trend in consumption reported in 2010 continued to exist throughout 2011 as well, although in slower paces.

For most of the Bulgarian smokers, their preferences for a given trademark are strongly influenced by its price.

During the past year, the efforts of Bulgartabac-Holding with regard to its pricing policy for the domestic market are directed towards stabilising and maintaining the market share of the Holding's leading brands within the separate price groups. In response to the reduced purchasing power of the population, a new format of cigarette pack was launched - cigarettes in packs of 10 pieces – a format which market share has increased constantly over the year and reached 7% of total sales of tobacco products in the territory of the country.

The competition is strong, with the cigarette factories in the country facing a constantly shrinking market. Moreover, the product we offer and sale is under a regime that imposes gradually various normative restrictions and other restrictive legal measures to limit smoking. Some of the companies started a price war by reducing the prices of its brands by 10 to 50 stotinki per pack.

- *Unregulated trade*

During 2011, the levels of offering and unregulated trade in tobacco products remained high. The levels of contraband offering of cigarettes and ROY tobacco of an unclear origin and quality remained the same. The sale of cigarettes with foreign excise stamps or without excise stamps is nation-wide and covers the entire territory of the country including the tiniest settlements.

According to data of an independent marketing agency, the excise market of tobacco products for 2011 has shrunk by almost 15% compared to the same period of 2010.

- *The financial and economic crisis*

The trend of decrease in sales of tobacco products with Bulgarian excise stamps applies to ours as well as to some of the competitor's cigarette brands. The significant fall of consumption of FMCG is due to the decreased purchasing power of the population, shrinking of households' expenses, the trend among smokers to reduce their smoking or even quit smoking completely.

Retailers experience some difficulties in ensuring the required working capital due on the one hand to the expensive credit resources and on the other hand to the significant decline in turnovers. This reflects on the range of tobacco products offered in the points of sale. Only the best selling brands are supplied in limited quantities to the shops with lower levels of turnover.

- *Distribution*

The marketing studies of the reporting period show that the distribution of Bulgartabac-Holding AD covers 96% of the points of sale of tobacco products in the country.

During the reporting period, the company updated the packing of the most sellable brand in Bulgaria - "Victory". Since March the family has been offered to the trade network in a new format and design. The new vision of the family "Victory" was supported by a large-scope marketing activity.

The brands of the Bulgartabac Group have a sustained nation-wide presence and in almost all points of sale, regardless of their size and importance.

Export of tobacco products

The trade policy of Bulgartabac-Holding AD for 2011 was directed towards the implementation of the main targets, set by the 2011 export program, namely:

- Increase of exported cigarette volumes;
- Expansion of markets where cigarette brands owned by Bulgartabac-Holding AD are being sold;
- Diversification and expansion of product portfolio for export;
- Increase of sales revenue per unit of produce;
- Selection of a strategic partner having a well-developed distribution network in each region;
- Development of blends in conformity with consumers' preferences in the respective regions;
- Finding the optimal forms for brands' establishment (promotional prices, marketing activities, etc);
- Collecting information on the main competitors in the region;
- Setting up of a product portfolio of brands enjoying legal protection within the respective region.

During the reporting period, the export policy of the Holding covered the targeted markets in the following regions: Middle East, Africa, Balkan countries, CIS, Far East, EU, Duty Free Zones.

During the past year of 2011, the export of Bulgartabac-Holding AD reached **15 648.85 million pieces**, while for the same period of 2010 it was **13 035.20 million pieces**. There is a growth of **20.05%** in the natural volumes. Respectively, in 2011 Blagoevgrad-BT AD manufactured and exported 7 462.795 million pieces vs. 6 661.28 million pieces in 2010, or a growth of almost 12.03%, while Sofia-BT AD manufactured and exported 8 186.056 million pieces in 2011 vs. 6 373.92 million pieces in 2010, or a 28.43% growth in volumes sold.

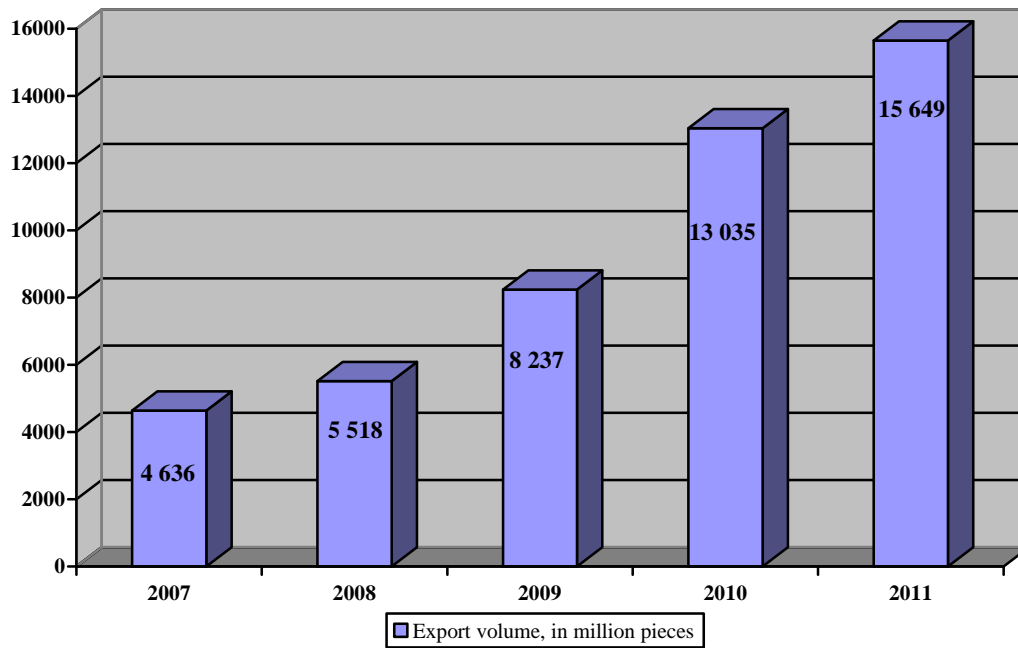
Sales in **2011** – 15 648.85 million pieces

Sales in **2010** – 13 035.20 million pieces

Volume growth (2011/2010) – 20.05%

(million pieces)

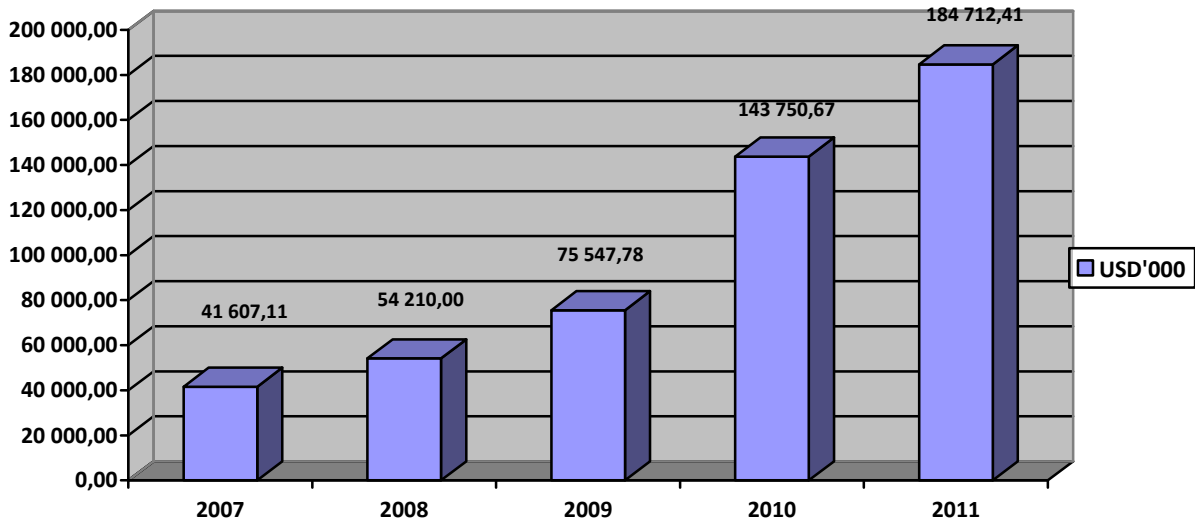
2007	4 636
2008	5 518
2009	8 237
2010	13 035
2011	15 649



Sales revenue for **2011** amounted to USD 184 712 407.44 and EUR 12 134 832.34 vs. USD 143 750 671.16 and EUR 12 532 126.44 for **2010**. Revenue in the period under review in USD, by factories, is as follows: Blagoevgrad-BT AD – USD 97 482 800 in 2011 vs. USD 83 010 178 in 2010, or a 17.43% growth; Sofia-BT AD – USD 87 229 607.44 in 2011 vs. USD 60 740 493.16 in 2010, or a 43.61% growth. Revenue in EUR, by factories, is as follows: Blagoevgrad-BT AD – EUR 1 679 554.00 in 2011 vs. EUR 1 349 204.00 in 2010, or a 24.48% growth; Sofia-BT AD – EUR 10 455 278.34 in 2011 vs. EUR 11 182 922.44 in 2010, or a 6.5% decline.

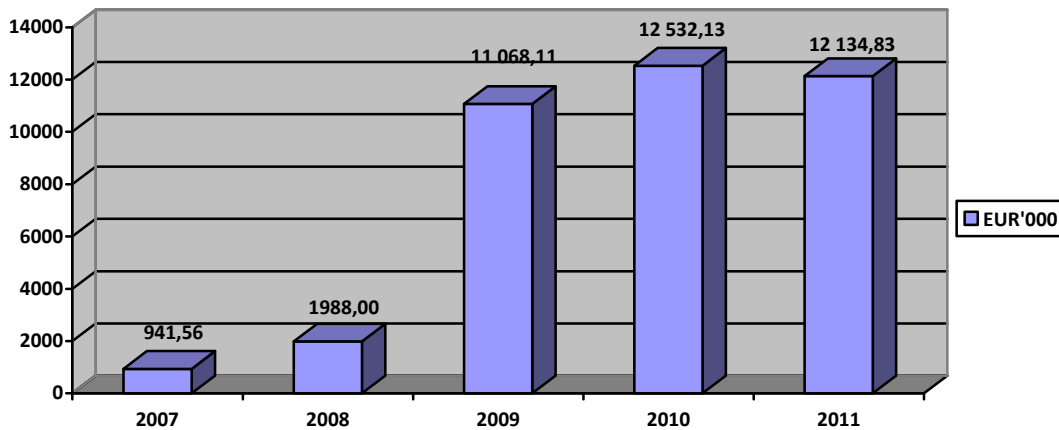
(USD'000)

2007	41 607.11
2008	54 210.00
2009	75 547.78
2010	143 750.67
2011	184 712.41



(EUR'000)

2007	941.56
2008	1 988.00
2009	11 068.11
2010	12 532.13
2011	12 134.83



Considering the above data, it may be concluded that **during 2011, despite of the gradual increase in export prices, the volumes sold are increasing compared to that sold during the same period of 2010.** Moreover, following the significant drop in sales for the Africa region in 2010 due to the termination of the production of brands owned by the client, the volumes of sales of brands owned by Bulgartabac-Holding AD has started to grow.

Based on the concluded trade representation contracts, Bulgartabac-Holding AD mediates in the overall process of negotiating, ordering and exporting the respective quantities of cigarette varieties by the subsidiaries. In relation to the above:

- Contracts were concluded and discussions were held with strategic partners operating well-developed distribution networks in each of the above-mentioned regions;
- The domestic competition of our brands offered in one and same region was successfully neutralised;
- During the last quarter of 2011, the negotiations were finalised and cigarettes were exported for the first time to Russia;
- The development of slims cigarettes 83mm for export continued;
- Bulgartabac-Holding AD made its cigarette production compliant to the requirements of Directive 2001/95/ EC of the European Commission on general product safety, which came into effect on 17 November 2011 by introducing the special quality of cigarette papers – LIP.

The results achieved so far are based on Bulgartabac-Holding AD's well-developed export portfolio for 2011.

- Well balanced – covering all possible formats and lengths in cigarette manufacturing – HLP (84 mm., 94 mm, 100 mm.), RC 84 mm., Slims 97 mm. (flap-flip top & octagonal), soft pack (84 mm.& 100 mm.);
- Optimal ratio “quality – price”;
- State-of-the-art design;

In the short-term run, the activity of Bulgartabac-Holding AD will be focused on the following activities:

- Identification of new markets for the company;
- Identification of changes in consumer demand on each of the existing markets as well as the consumer characteristics of the new ones;
- Continued development and updating (customisation) of the portfolio - entirely customer-oriented;
- Development of cigarettes super slims 83 mm for export.

The objective analysis of the markets and potential of our brands reveals that it is quite possible to achieve sales volumes in foreign markets in 2012 of 17 066 510 thousand pieces, or a 9% growth compared with the volumes sold in 2011.

➤ **Auxiliary materials and spare parts**

The main target in 2011 was to provide the subsidiaries with auxiliary materials and spare parts in order to ensure the implementation of their production programs.

During the period under review, aiming at achieving the goals for maintaining the best possible prices and terms of delivery of auxiliary materials, the practice to enlarge the scope of companies-suppliers and to carry out production testing at subsidiaries for approval of the qualities of at least three suppliers for each material as to avoid monopolization of supplies by one supplier was continued.

Events directly related to this activity and having an impact on the financial results were in the following fields:

In view of the drastic raise of PP resin prices – the main raw material for PP foil production and the increase of PP foil world prices, the foil prices are by approx. 3% to 5% higher than that in 2010.

Considering the increased consumption in 2011 of stiff cardboard for recess filters production, a 5% discount was agreed upon when reaching certain annual quantities. The levels of supply prices of stiff cardboard in Q'4 of 2011 were 9% lower as compared to the same period of 2010.

Despite the raise in cellulose prices, upon negotiations, we managed to agree on prices for the supply of cigarette paper, wrapping paper and tipping paper for the Q'4 of 2011 that are by about 3% lower on the average that the prices at the beginning of 2010.

The price of inner frame cardboards has decreased by 2.6% to 4.5% compared to the average 2010 prices.

In 2011 the trend of limited supply of acetate tow in the global market continued due to the higher demand and shortage of raw materials.

Production capacities of all manufacturers are filled up and in view of the increased prices of cellulose in the international markets, the prices for tow delivery in 2011 have increased by approximately 4 - 5% compared with that in 2010. However, a reduction by 1% in the price of quantities supplied during 2011 was achieved with one of the suppliers of acetate tow.

Recess filters – despite of the increased prices of acetate tow, the main raw material for the production of filters, after negotiations held a decrease of 1.5% in the prices for Q'4 was agreed compared with the levels at the beginning of the year.

The analysis of the period under review revealed an increase in price of Tryacetin by 8% to 10% and maintaining their 2010 levels for the other chemical products - propilenglikol and glycerine.

The prices of printing products had decreased from 7.5% to 10.3%. The decrease in the prices of glues and aluminium foil was by 3-4%.

A significant decrease was achieved in the price of one of the main aroma products - 20-23% and 5% of the price of the total quantity supplied in 2011 to both subsidiaries – Blagoevgrad-BT AD and Sofia-BT AD.

In connection with Directive No 2001/95/EC for safety of goods of the European Union and the introduction of Standard EN 16156, as of 17 November 2011 all cigarettes to be sold in the domestic market and in the markets of the EU Member States must be produced using a LIP cigarette paper.

The subsidiaries commenced the production of cigarettes with this quality of paper in the end of September. This trend will continue in the future as well.

Fees to Bulgartabac-Holding AD under contracts for trade representation in Intra Community Acquisitions and Imports of auxiliary materials	
<i>31.12.2011</i>	<i>31.12.2010</i>
BGN 876 thousand	BGN 638 thousand

The activity on ensuring the production process with spare parts is carried out through making orders to the designated supplier of the company – manufacturer of the respective plant and equipment.

Fees of Bulgartabac-Holding AD under contracts for trade representation in Intra Community Acquisitions and Imports of spare parts	
<i>31.12.2011</i>	<i>31.12.2010</i>
BGN 113 thousand	BGN 75 thousand

➤ **In the area of technological policy, recipes and blends**

During Q'4 of 2011 activities aimed at securing cigarette manufacturing with tobaccos and reconstituted tobacco, technological developments for adapting cigarette blends to the technology of drying and expansion of cut tobacco, commencement of the production of self extinguishing cigarettes with the aim of their introduction to the market, implementation of technological projects for the development of super slims cigarettes and design of cigarettes for export were carried out.

Provision of tobaccos and reconstituted tobacco for the production.

1. Visual assessment and selection of samples of Virginia tobacco, origin USA, Malawi, Zimbabwe, and Italy; and of Burley tobacco, origin USA, Italy, and Argentina, as also Maryland tobacco, MPA class, USA, were carried out. Taste evaluations and chemical analyses of all selected samples were carried out as well. Approved for reservation were quality groups of Virginia tobacco, origin USA and Italy, crops 2010 and 2011, and of Burley tobacco, origin USA and Argentina. A specification of the approved samples and their allocation together with a schedule for supply of tobaccos by classes and suppliers were drawn up with the aim to cover the needs of cigarettes manufacturing for 2012.

2. In order to secure the cigarette production with Bulgarian Virginia tobacco, crop 2011, an analysis and evaluation of the quality of tobacco bought-up by Pleven-BT AD were carried out. Based on the visual and taste evaluation and chemical indicators, specialists of Bulgartabac-Holding AD, Blagoevgrad-BT AD and Sofia-BT AD prepared and coordinated with Pleven-BT AD terms of reference for the processing of Virginia tobacco, crop 2011.

Tobacco processing commenced at Pleven-BT AD and batches were prepared of the two approved Virginia tobacco classes, based on which technological control was exercised over the production, as also a taste evaluation and chemical analysis of control samples were carried out.

3. Taste evaluations and chemical analyses of regular samples of reconstituted tobacco, quality AZ6N of "LTR", France, were made. A statement of the required quantities of reconstituted tobacco, quality AZ6N France was drawn up with the aim to secure the cigarette production in 2012.

Technological developments

1. Implementation of a technology for drying and expansion of cigarette blends cut tobacco at Sofia-BT AD.

The recipes of cigarette brands produced at 50% and 100% cut tobacco expansion were updated and customised. Production monitoring was provided upon drying and expanding cut tobacco and the effectiveness of the processing of tobacco blends of different qualities was measured. Chemical analyses and taste evaluations of currently manufactured cigarettes were carried out. The physical indicators of cigarette blends manufactured by Sofia-BT AD were optimized in accordance with the achieved effect of brand expansion.

2. Dossiers of new varieties of cigarette brands produced by Sofia-BT AD for clients of the

Holding and for export were developed and approved.

3. In Sofia-BT AD and Blagoevgrad-BT AD commenced the production of self extinguishing cigarettes – brands intended for sale in the domestic market and for export to the markets of the EU Member States. Production tests were carried out with new qualities of cigarette paper with lower ignition propensity (LIP). A comparative evaluation of the quality was carried out – chemical indicators and taste evaluation of cigarettes manufactured using LIP cigarette papers supplied by various suppliers. Tests of cigarettes under the ASTM method were carried out with the purpose to assess their compliance with the requirement for extinguishment. The reported results were in line with the normative requirements of the European Standard EN 16156:2010.

4. In order to improve smoking and taste qualities of American blend cigarettes, an evaluation and production testing of a new casing for toasting Burley tobaccos were carried out at Blagoevgrad-BT AD.

Development of cigarettes “super slims”, 83 mm

Two tobacco blends were developed and production tests were carried out of cigarettes “super slims” 83 mm, in the direction of Virginia and American blend. New qualities of additions were used – casing and aroma compositions; a taste evaluation and chemical indicators of sample cigarettes were carried out.

The developed cigarette “super slims” blends, 83mm, are of smoking and taste characteristics approved for specific markets; they have been produced in varieties with different levels of smoke indicators.

➤ **Quality Management System**

During the reporting period, the process of maintenance and development of the Quality Management System (QMS) of Bulgartabac-Holding AD in accordance with the requirements of ISO 9001:2008 continued. The decisions of management and the implementation of specific recommendations in relation to the system’s development were subject to periodical reviews. The work with the two working groups New assortments – blend and design on implementing new developments pursuant to the requirements of the Standard continued as well.

It was scheduled in the QMS audit plan that AFNOR International Bulgaria would carry out a supervisory audit on 6 October 2011. The preparation commenced by drawing up reports on the fulfilment of quality goals by directorates, departments, and units. Client satisfaction reports were drawn up, as well as reports on the activities with clients. The above reports indicated that there were no claims against the company and it worked well with its clients. The summarized reports and statements on the fulfilment of quality goals reported that the half-year goals were accomplished.

The supervisory audit held on 6 October 2011 by AFNOR International Bulgaria concluded that the Quality Management System of Bulgartabac-Holding AD was applied in compliance with the requirements of the Standards, and there were no inconsistencies. The recommendations made in the course of the certification audit held in 2010 were implemented.

An important task in maintaining the required competence of internal auditors is their periodical training. It has been reported that the updated QMS published in the intranet of Bulgartabac-Holding AD is used.

The well operating Quality Management System of Bulgartabac-Holding AD is an additional quality assurance tool that is provided to our clients.

3. Analysis of the financial status and financial result of Bulgartabac Holding AD as of 31 December 2011

Bulgartabac Holding reports net profit from its operation during the financial year 2011 in the amount of 31 851 thousand leva, which represents a significant increase compared to its net profit during 2010 in the amount of 5 825 thousand leva (+ 26 026 thousand leva).

The key drivers of the improved financials are the increased royalty and fees income, combined with the increase in the dividends paid out by the two cigarette production companies – “Sofia – BT” AD and “Blagoevgrad – BT” AD.

As a result of the successful trade policy in 2011 Bulgartabac Group increased the sale volumes of cigarettes substantially:

	2011	2010	+/- mln. sticks	+/- %
“Sofia –BT” AD cigarettes volume (Mln. Sticks)	9 895	7 594	2 301	+30,30 %
Local Market	1 709	1 220	+489	+40,08 %
Export	8 186	6 374	+1 812	+28,43 %
“Blagoevgrad – BT” AD cigarettes volume (Mln. Sticks)	9 789	8 557	1 232	+14,40 %
Local Market	2 327	2 290	+37	+1,62 %
Export	7 462	6 267	+1 195	+ 19,07 %

The growth in the sales of the subsidiaries (due to increased volumes and prices) is directly related to the 21,28 % increase of the reported royalty income and the 12,43 % increase of the reported trade representation fees (commissions) of Bulgartabac Holding.

The comparative analysis of the income reveals the following tendencies

Income	2011	2010	+/- 000' BGN	+/- %
Dividend paid by subsidiaries	32 035	1108	+30 927	+2 791,25 %
Royalty	13 173	10 862	+2 311	+21,28 %
Fees	9 722	8 647	+1 075	+12,43 %
Incl. fees on export of cigarettes	7 270	6 882	+388	+5,64 %
Incl. fees on import/export of	1 437	1037	+400	+38,57 %

tobacco				
Incl. auxiliary materials and spare parts	989	713	+276	+38,71
Sales of tobacco	7 293	21 433	-14 140	-65,97 %
Interest and penalties on loans	17	27	-10	-37,04 %

The only operational revenue stream that is reported to decline in comparison to 2010 is the income from sale of tobacco which is a result in the delay of the purchase and industrial processing of the crop 2010. This effect corresponds to the increased inventory of finished products (increased by 16 496 thousand leva).

The costs were broadly in line with last year. Notable changes are reported in the following expense items:

1. Hired services related to marketing activities – in an attempt to support sales in a very competitive market, the reported market expenses increased by app. 15 % (786 thousand leva).
2. Personnel expenses are reported to increase by 5 % (452 thousand leva) as a result of severances paid.

The sustainability and viability of the company are depicted by the following key financials

Financials	2011	2010	2009
Price /Earning (P/E)	7,25	38,98	39,35
Market capitalization / sales (P/S)	3,71	5,39	3,09
Price / Balance sheet value (P/B)	3,18	2,41	1,39
Return on equity (ROE)	43,88 %	6,21 %	3,54 %
Return on assets (ROA)	40,81 %	5,86 %	3,09 %
Earnings before interest and taxes (EBIT) 000' BGN	31 846	6 356	2 733
(ROE using EBIT)	43,88 %	6,78 %	3,03 %

(ROA using EBIT)	40,80 %	6,39 %	2,64 %
Market capitalization/ EBIT (P/EBIT)	7,25	35,70	46,01
Debt-Equity ratio	0,08	0,06	0,15
Liquidity ratio	12,26	17,35	6,04
Assets - Turnover	0,80	0,42	0,39

4. Major risks and uncertainties faced by Bulgartabac-Holding AD in 2011

Analysis of the conditions in which Bulgartabac-Holding AD will work during 2011

Political factors

- Strong political will for the privatization of Bulgartabac-Holding AD;
- Legislative changes concerning the manufacturing, storage and sales of excise goods on the territory of the country;
- Presidential and local elections in 2011;
- Legislative measures for restriction of tobacco smoking and advertising of cigarettes;
- Ambition of the Government to apply anti-crisis measures and incentives that should lead to positive trade balance of the country already during 2011;
- Political changes in some Arab countries, which have brought about an increase of the price of petrol in the beginning of 2011.

Economic factors

- Gradual transition of the Bulgarian economy to a model of development, in which export is the main growth factor;
- Increased excise rates of cigarettes (during 2011 only for the sizes that are not manufactured by Bulgartabac Group) and of roll-your-own tobacco - from BGN 100/kg to BGN 130/kg (2011);
- Considerable share of sales of cigarettes without excise stamp or with foreign excise stamp in the country;
- Expected increase in prices of basic raw materials due to the appreciation of petrol;
- Increased sensitivity of the cash flows of the cigarette manufacturing companies of Bulgartabac Group due to the fluctuations of the USD exchange rate against that of the other world's currencies.

Social Factors

- Worldwide social and health policy of fighting tobacco smoking;
- Restrictive law on smoking in public places and restaurants;
- Drop in employment, although with subsiding rate of reduction, due to the continuing process of restructuring of the companies in the country;

- Binding the policy on income growth with the growth of labour productivity and the potential of the economy and the budget of the country;
- Potential threat of social tension with the progress of the process of privatization and restructuring of Bulgartabac-Holding AD;
- Need to cut down expenses, including personnel expenses, which also lead to the respective negative social consequences.

Technological factors

- Legislative restrictions on advertising and marketing of tobacco products, leading to intensification of the competition among manufacturers in the area of quality, sizes and outer appearance of the products and, respectively, to introduction of still newer technologies;
- Production of self extinguishing cigarettes (LIP paper) for the brands to be sold on the territory of EU starting as of 17 November 2011;
- Bulgartabac Group companies have modern technological equipment at their disposal which guarantees the manufacturing of high quality competitive products and enables them to develop and update their product ranges, in conformity with market trends;
- Consistent policy regarding the outer appearance of the products of Bulgartabac Group.

Other risks factors **inherent** to the company's activity may be reviewed in the following directions:

Risk factors specific to the Growing and Buying-up of Raw Tobacco Sector

The membership of Bulgaria in the EU has led to dynamic changes in the development of the Raw Tobacco Growing Branch in the country and the legislative mechanisms of tobacco buy-up and processing.

1. Starting with crop 2010 the Minimum purchase prices of raw tobacco, earlier being fixed each year by the Council of Ministers, were eliminated. Tobaccos of the crop were bought-up at market prices determined by each licensed company.
2. By issue 19 of the State Gazette of 08 March 2010 Articles 11, 16 and 33 of the Tobacco and Tobacco Products Act were repealed as also the texts of the Act related to the repealed articles. The main changes are as follows:
 - liberalization of the raw tobacco market – this will lead to significant changes in the organization of the process of buying-up of this raw material with many “small” buyers that do not have permits for tobacco processing penetrating the market. This change is forecasted to have a lower impact on the tobacco processing companies operating in the country;
 - the obligation to carry out the tobacco processing within the territory of the country was eliminated;
 - the imperative regulation of the Tobacco and Tobacco Products Act for conclusion of contracts between the tobacco growers and the purchasers of raw tobacco was abolished.

The production of Basma variety group was the most affected by the liberalisation of the raw tobacco market. The overall production volumes were reduced by about 30% compared with the previous crop, which, when combined with the relatively higher quality of the crop, has led to an increase in the purchase prices of the raw tobacco. A higher price is observed also for the variety groups Burley and Kaba Koulak, whereas the production volumes were kept within those produced in the previous year. An estimate could be made that the market of raw tobacco of these three variety groups will continue being unstable in the short-term and mid-term run in view of

the large number of growers. Due to the relatively lower number of growers of Virginia tobacco, there is a balance between the market demand and supply with regard to this type of tobacco.

Risks in the area of tobacco trade

Tobacco supply in 2011 was directed mainly to tobacco dealers operating in the sector, thus on the one hand allowing the maintenance and activation of export possibilities, and on the other hand reducing significantly existing trade risks. Risks related to payment of tobacco sold were cut down to the minimum and no tobacco deliveries were made under deferred payment conditions to markets and firms at risk.

Risks related to investing in shares of the Company

Bulgartabac-Holding AD is a registered public company whose shares are listed for trading on the Unofficial Market of Bulgarian-Stock-Exchange-Sofia AD, segment A. The market value of shares offered is determined on the basis of demand and supply and their price is dependent on both the economic and financial results of the company and information being announced publicly by the company, as also by the common factors having impact on the capital market in the country.

The company cannot guarantee that there will not be any fluctuations in prices of its shares. In a number of cases, these fluctuations neither relate nor correspond to the operating results of the company and therefore, they cannot be predicted.

Bulgartabac-Holding AD was included, effective 21 March 2011 in the database of two stock exchange indices: **BG TOTAL RETURN 30** and **BG 40**.

BG TOTAL RETURN 30 is an index based on the price performance of the common shares included in the index portfolio. It comprises the biggest and most liquid 30 companies traded in BSE-Sofia classified in accordance with a number of criteria, each one having equal weight: market capitalization, number of transactions during the last 6 months, turnover during the last 6 months, and free-float.

BG 40 is an index based on the price performance of the issues and comprises 40 issues of common shares of the companies with the greatest number of transactions and the highest median value of the daily turnover during the last 6 (six) months as the two criteria shall have equal weight.

Financial risk management

In the ordinary course of its business activities, the company is exposed to a variety of financial risks the most important of which are market risk (including currency risk, interest rate risk and other price risk), credit risk and liquidity risk. The general risk management is focused on the difficulties of forecasting the financial markets and minimizing the potential negative effects that might affect the financial results and position of the company. The financial risks are currently identified, measured and monitored through various control mechanisms introduced in order to establish adequate prices for the services, provided by the company, to appropriately assess the market circumstances related to its investments and the forms for maintenance of free liquid funds through preventing undue concentration of a particular risk.

Risk management in the company is currently executed by the management and the respective structural units, depending on the type and specific features of various risks to which the company is exposed in its operations.

Financial risk management is described in detail in the notes to the interim financial statements as of 31 December 2011.

5. Information about large-scope transactions concluded among related parties

During **the fourth quarter of 2011** Bulgartabac-Holding AD did not have any significant transactions with related parties.

During **the third quarter of 2011** Bulgartabac-Holding AD concluded contracts with Blagoevgrad-BT AD and Sofia-BT AD, as follows:

- Contract dated 30 June 2011 with Blagoevgrad-BT AD for the sale of tobacco of variety group Burley – strips, crop 2010, for the amount of BGN 1 259 thousand (VAT excluded). The contract was completed in July 2011.
- Contract dated 30 June 2011 with Sofia-BT AD for the sale of tobacco of variety group Burley – strips, crop 2010, for the amount of BGN 1 717 thousand (VAT excluded). The contract was completed in August 2011.

On the grounds of Art.100o, para.7 of POSA we hereby inform that the interim financial statements as at 31 December 2011 of Bulgartabac-Holding AD have not been certified and audited.

Angel Dimitrov
Executive Director
of Bulgartabac-Holding AD

Ventsislav Cholakov
Executive Director
of Bulgartabac-Holding AD