

LPP S.A.

Report supplementing the opinion from the audit of the financial statement for the reporting period between 1st January and 31st December 2003

I. Company overview

- (a) LPP S.A., hereinafter referred to as the Company, runs its business in compliance with the Polish Code of Commercial Partnerships and Companies. The Company's registered office is located in Gdańsk at ul. Łąkowa 39/44. Apart from its registered office, the Company also runs its business in Company-owned warehouses in Pruszcz Gdański. The sales are run in 3 wholesale outlets and 41 brand stores located across Poland.
- (b) The Company's notarial Deed of Association was drawn up in the Notarial Office in Gdynia on 7th December 1989, Repertory A no. 2452/1989. On 18th December 1989, the Company was registered by decision of the District Court in Gdańsk in the Commercial Register, RHB entry no. 3878. By decision of the District Court in Gdańsk, the Company was entered in the National Court Register, entry no. KRS no. 00000778. The last updated copy of the Company's entry in the National Court Register was prepared on 15th January 2004.
- (c) The Company's tax identification number (NIP) is 583-10-14898 and its statistical identification number (REGON) is 190852164.
- (d) The Company's basic objects, according to its Statute, are wholesale and retail sale of clothing.
- (e) The Company's financial statement for the previous reporting period between 1st January 2002 and 31st December 2002 has been audited by Moore Stephens Trzemzański, Krynicki i Partnerzy Kancelaria Biegłych Rewidentów Sp. z o.o. with its registered office in Gdańsk, at ul. Rogaczewskiego 9/19 and an unqualified audit opinion was issued.
- (f) The Company's financial statement for the previous reporting period has been approved by resolution of the General Meeting of Shareholders held on 27th June 2003. On 28th June 2002, the General Meeting of Shareholders distributed the entire net profit for the previous fiscal year of PLN 18,556,165.95 and decided to transfer the entire amount to the reserve capital.
- (g) The financial statement for the previous reporting period was filed with the National Court Register on 16th July 2003 and filed for publication in *Monitor Polski B* (Official Journal) on 11th July 2003 and published in *Monitor Polski B* no. 18 of 15th January 2004.
- (h) The Company's authorities are: the General Meeting of Shareholders, the Supervisory Board and the Management Board.
- (i) Composition of the Supervisory Board in the audited period was as follows:
- Jerzy Ryszard Lubianiec Chairman of the Supervisory Board
- and the following members:
- Maciej Krzyżanowski – until 27th June 2003
 - Grzegorz Słupski
 - Wojciech Olejniczak
 - Sławomir Łoboda – until 27th June 2003
 - Bogdan Małachwiej

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- Jacek Siwicki – since 27th June 2003
- Krzysztof Faferek – since 27th June 2003

Composition of the Company's Management Board in the reporting period was as follows:

- Marek Piechocki President of the Management Board
- Dariusz Pachla Vice President of the Management Board
- Alicja Milińska Vice President of the Management Board
- Stanisław Dreliszak Vice President of the Management Board

(j) As at the balance sheet date, the Company's share capital amounted to PLN 3,407,000 and was divided into 1,703,500 shares of nominal value PLN 2 per share. As at the balance sheet date, the Company's shareholder's equity amounted to PLN 158,280,894.69.

(k) Allocation of the Company shares as at the balance sheet date was as follows:

		Number of shares	Value of shares in PLN	% of votes held
Marek Piechocki	President of the Management Board	281,428	562,856	31.62
Jerzy Lubianiec	Chairman of the Supervisory Board	279,327	558,654	31.56
Grangefont Polish Enterprise Fund IV,L.P.	London	350,000	700,000	11.28
Other		215,000	430,000	6.93
		577,745	1,155,490	18.61
		1.703.500	3,407,000	100.00

(l) The Company's share ownership structure has changed in the reporting period, also as a result of the issue of 190 000 new Company shares targeted at and taken hold of by small and medium-sized investors. The percentage of shareholders holding less than 5% of votes in the total number of votes at the General Meeting of Shareholders increased from 13.9% to 18.6%.

(m) The Company's related parties are listed in the Notes to the financial statement. They include 18 subsidiaries based in Gdańsk and 6 foreign subsidiaries based in Estonia, Latvia, Lithuania, the Czech Republic, Hungary and Ukraine.

(n) The current reporting period includes 12 consecutive months from 1st January 2003 to 31st December 2002. The previous reporting period includes 12 months of 2002. The reporting period from two years ago includes 12 months of 2001.

II. General audit information

(a) Pursuant to resolution of the Management Board of 3rd April 2003, Moore Stephens Trzemzałski, Krynicki i Partnerzy Kancelaria Biegłych Rewidentów Sp. z o.o. has been appointed the Company's certified auditor, upon approval of the Supervisory Board expressed in the resolution of 3rd April 2003.

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- (b) The audit was conducted at the Company's registered office on the basis of the contract concluded on 3rd April 2003 between the Company as the Contracting Party, and Moore Stephens Trzemżalski, Krynicki i Partnerzy Kancelaria Biegłych Rewidentów Sp. z o.o. with its registered office in Gdańsk at ul. Rogaczewskiego 9/19, as the Contractor, between 9th February and 31st March 2004.
- (c) In the audited period, the Company performed a stock-take of:
- by way of physical inventory count:
 - cash in hand as at 31st December 2003;
 - inventory in warehouses and brand stores was counted at various dates in 2003 at appropriate intervals;

 - - by way of statements of account received from banks and trading partners:
 - cash in banks as at 31st December 2003;
 - financial assets as at 31st December 2003;
 - receivables as at 31st December 2003;

 - by way of comparison of accounting books against relevant documents:
 - land as at 31st December 2003;
 - fixed assets in progress as at 31st December 2003;
 - intangible assets as at 31st December 2003;
 - financial assets as at 31st December 2003;
- The auditor supervised the stock-take of goods in the Reserved brand store located in the shopping mall CH Madison in Gdańsk as at 4th December 2003. The inventory value determined in the stock-take equalled PLN 216,000. According to the auditor, the stock-taking procedures were appropriate.
- (d) No findings and conclusions of any external auditing institution were used in the audit and in the preparation of this report.
- (e) A written statement of the Company's legal advisor was issued on 15th February 2004, setting forth all litigation procedures and legal matters related to the Company.
- (f) On 1st April 2004, The Company's Management Board provided the auditors with a statement confirming completeness, reliability and accuracy of the financial statement to be audited, as well as disclosure of all contingent liabilities in the Notes to the financial statement and non-existence or possible existence of events which could impact the data presented in the financial statement for the audited year to a material extent (by the end of completion of the audit).

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III. Audit summary

In comparison with the previous year, the basic financial ratios are good. Financial analysis presents positive changes in liabilities; the share of shareholder's equity in the structure of operations financing increased by 20%, along with the corresponding decrease in external capital employed. Increase in sales, ROS and net profit, as well as the increase in balance sheet total indicate that the upturn trend in the Company's development continues.

Results of the audit of the Company's financial statement and the analysis of financial ratios do not indicate any hazard to the Company's going concern in 12 months after the balance-sheet date.

However, the impact of factors highlighted by the Management Board in the report on the Company's performance must be taken into account. Final financial results of the following reporting period may be impacted by other factors, including without limitations the exchange rates of USD and EURO, which should determine the level of costs related to rent of commercial premises.

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IV. Financial analysis

BALANCE SHEET as at 31st December 2003

	Note	A End of current period PLN '000	B End of previous period PLN '000	Change (A-B) PLN '000	Change (A-B)/B %	End of current period Structure %	End of previous period Structure %
ASSETS							
Fixed assets							
Intangible assets	1	6 328	978	5 350	547%	3%	1%
Tangible fixed assets	2	65 256	40 528	24 728	61%	27%	24%
Long-term receivables	3	396	210	186	89%	0%	0%
Long-term investments	4	6 986	3 141	3 845	122%	3%	2%
Long-term prepaid expenses	5	2 105	3 163	-1 058	-33%	1%	2%
		81 071	48 020	33 051	69%	33%	29%
Current assets							
Inventory	6	87 092	76 603	10 489	14%	36%	46%
Short-term receivables	7,8,9,10	40 028	34 304	5 724	17%	16%	21%
Short-term investments	11	28 380	7 004	21 376	305%	12%	4%
Short-term prepaid expenses	12	6 343	890	5 453	613%	3%	1%
		161 843	118 801	43 042	36%	67%	71%
Total assets		242 914	166 821	76 093	46%	100%	100%

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BALANCE SHEET as at 31st December 2003 (continued)

BALANCE SHEET as at 31st December 2003						
			A	B		
			End of	End of		
			current	previous	Change	Change
	Note		period	period	(A-B)	(A-B)/B
			'000 zł	'000 zł	'000 zł	%
LIABILITIES						
Shareholder's equity						
Share capital	13		3 407	3 027	380	13%
Unpaid share capital			0	0	0	0%
Treasury shares			0	0	0	0%
Reserve capital	14		118 152	50 669	67 483	133%
Revaluation capital			0	0	0	0%
Other capital reserves			0	0	0	0%
Profit (loss) from previous years			2 442	2 442	0	0%
Net profit (loss)	VI		34 280	18 556	15 724	85%
Write-offs from profit made during the fiscal year				0	0	0%
			158 281	74 694	83 587	112%
Liabilities and provisions for liabilities						
Provisions for liabilities	15		1 312	470	842	179%
Long-term payables	16		5 326	7 344	-2 018	-27%
Short-term payables	17,18,19		75 056	82 744	-7 688	-9%
Accruals and deferred income	21		2 939	1 569	1 370	87%
			84 633	92 127	-7 494	-8%
Total liabilities			242 914	166 821	76 093	46%

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PROFIT AND LOSS ACCOUNT (nature format)
for the fiscal year between 1st January and 31st December 2003

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The Company's assets and financial standing, financial result, and profitability.

The Company's operations, financial results and profitability in the fiscal year, as well as its assets and financial standing as at the balance sheet date against the previous period is summarised by the following ratios:

- payables turnover	$\frac{\text{average short-term payables} \times 365 \text{ days}}{\text{operating expenses}}$	days	147	109
- equity to fixed assets ratio	$\frac{\text{shareholder's equity}}{\text{fixed assets}}$		1,95	1,56
financing structure	$\frac{\text{shareholder's' equity} + \text{long-term payables}}{\text{total liabilities}}$		0,67	0,49
			End of current period	End of previous period
<u>Liquidity ratios</u>				
- liquidity ratio I	$\frac{\text{total current assets}}{\text{short-term payables}}$		2,16	1,44
- liquidity ratio II	$\frac{\text{total current assets} - \text{inventory}}{\text{short-term payables}}$		1,16	0,51

V. Description of selected items presented in the financial statement

1. Intangible assets

Intangible assets include mainly software licences. The major reason behind their increase against the previous period is the acquisition and advance payment for the retail sale management IT systems.

2. Tangible fixed assets

This item includes mainly the net value of buildings and upgrade of buildings not owned by the Company, presented in the financial statement. The increase against the previous period can be attributed to the acquisition of new fixed assets (by groups). Expensed outlays in brand stores (in external funds) represent 68% of the item A II 1.6 under Assets in the Balance Sheet. Under long-term contracts of lease, the Company has the right to use these outlays.

3. Long-term receivables

Long-term receivables include mainly contractual deposit payments related to future deliveries of equipment (furniture) to brand stores, and security payments under contracts of lease of commercial premises.

4. Long-term investments

These are financial assets. The main items are shares contributed to subsidiaries and loans granted. Valuation of outlays expensed in subsidiaries is presented in item 21 in the Note to financial statement. No reservations are made to conclusions presented therein.

5. Long-term prepaid expenses

Long-term prepaid expenses mainly include deferred income tax assets and other prepaid expenses related to the cost of increase in the Company's share capital in previous years, allocated in time.

6. Inventory

The main item here are goods. Increase in their value against the previous period totals approx. 14% and is lower than sales growth. The structure of goods by marketability is as follows

- | | |
|---|-------|
| • goods at wholesaler's and in brand stores | 36.9% |
| • goods in bonded warehouses | 23.6% |
| • goods en route to bonded warehouses | 39.5% |

Inventory items referring to previous sales seasons have been identified. A relevant revaluation write-down has been made for items whose forecast net selling prices are lower than their purchase price.

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7. Short-term receivables

The time structure of the main short-term receivables by their maturity has been presented in the Notes to the financial statement. Receivables in foreign currencies have been valued as at the balance sheet date in line with regulations currently in force.

8. Trade receivables

Increase in trade receivables against their balance as at the end of the previous fiscal year is identified mainly in the item "trade receivables due from related parties". No claimed receivables and overdue receivables are included in this group. Claimed and overdue receivables due from other entities amounted to PLN 24,743,000; relevant revaluation write-downs were made in the amount of PLN 6 082 000.

9. Receivables due under taxes, subsidies, customs duties and social insurance

This item includes overpayment of tax on transport vehicles for 2003.

10. Other receivables

The main items here are settlements related to contractual deposits made and total calculated Value-Added Tax to be settled against the budget in January 2004.

11. Short-term financial assets

As at the balance sheet date, the Company owns the following short-term financial assets:

- loans granted 27.0%
- bank deposits and other cash 29.1%
- cash in hand and cash in banks 43.9%

12. Short-term prepaid expenses

The major item here (77% of the total value) are costs related to licenses and preparation of IT system to be implemented. Relevant works are in progress, and the expected date of their acceptance for use is April 2004.

Other items include prepaid costs of OC and AC insurance (third party insurance and accident and theft insurance) and property insurance related to future periods, as well as the costs of increase in the Company's capital incurred in previous years and allocated in time.

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13. Share capital

In the reporting period share capital was increased (as described in the statement of changes in shareholders' equity).

Share capital was paid for in cash in the amount of PLN 3,293,600, and in kind in the amount of PLN 113,400.

14. Reserve capital

Changes in reserve capital are presented in the statement of changes in shareholders' equity. The increase in shareholders' equity in the reporting period is the write-off from profit from the previous year and inflows from the issue of shares above their nominal value.

15. Provisions for liabilities

These include provisions for the deferred income tax and for holiday leaves not taken (established and reversed in due manner), as well as a calculated provision for retirement severance payments determined by the Polish Labour Code.

16. Long-term payables

These are related to two bank credits, and are considered investments; both are to be paid for year on year.

17. Short-term payables – time structure by maturity as at the balance sheet date

The time structure of the main short-term payables by their maturity as at the balance sheet date has been presented in the Notes to the financial statement. Payables in foreign currencies have been valued as at the balance sheet date in line with regulations currently in force.

18. Short-term trade receivables

There are no major overdue payables in the total value of short-term trade payables. 97% had been paid by the audit date.

The Company's losses related to interest due under these payables are immaterial, and no provisions for future payables are established.

19. Payables due under taxes, subsidies, customs duties and social insurance

Types of budget payables are presented in the Notes to the financial statement.

In the current reporting period the Company has not been inspected by fiscal authorities.

Within the total liabilities, the amount of income tax payable to the budget for 2003 is material. Its date of maturity is 31st March 2004. All payables have been paid and settled in due time.

20. Other short-term payables

The main item here are Special Funds, including the Company Social Fund and the Company Fund for Rehabilitation of the Disabled. The Company deposits relevant funds on a separate bank account in the required amounts. The funds are established and used in line with current regulations.

Other payables include settlements with employees settled before the audit date and due VAT to be settled with the budget in the following period.

21. Accruals and deferred income

Major items here are:

- subsidies from the Company Fund for Rehabilitation of the Disabled used for the preparation of workplaces for the disabled, less depreciation write-downs of fixed assets acquired with these subsidies,
- claims for damages.

22. Collaterals established on assets to the benefit of third parties

- To secure repayment of investment credits, a mortgage has been established on the Company's real estate in Gdańsk and Pruszcz Gdański.
- Claims for damages; revolving credits are secured by way of registered pledges on goods and the transfer of ownership rights to goods.

The amount of these collaterals is presented in the Notes to the financial statement.

These elements of assets are at unlimited disposal of the Company.

23. Net revenues from sales and their equivalents

The Company's core business in the current period is trade of clothing – sales of clothing represents the major part of generated revenues.

Sales of services contributed to the revenue generated in the current period to a lesser extent.

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The share of export sales within the total sales remains stable, although its value increased by over PLN 12 million.

Total revenues from sales has increased significantly against the previous reporting period, which was caused by the further expansion of the retail stores network

24. Operating expenses

The main item under the operating expenses is the prime cost of goods sold. Its increase against the previous year is slower than the growth of sales; as a result, higher gross profit margin was generated and profit on sales increased.

Generic costs whose growth is higher than the average ratio of operating expenses growth include: amortisation and depreciation, outsourced services, salaries and social insurance. Increase in costs of labour is a result of increased headcount against the previous year.

25. Other operating revenues and expenses

Other operating revenues and expenses are listed in the Notes to the financial statement. They are duly documented and classified.

26. Other financial revenues and expenses

Other financial revenues and expenses are listed in the Notes to the financial statement. They are duly documented, classified and qualified.

27. Income tax

Discrepancies between the gross balance sheet total and the income and tax base are presented in the Notes to the financial statement.

The income tax presented in the profit and loss account includes the tax due for 2003 and immaterial adjustment of the income tax for 2002.

Presentation of changes in provisions and deferred income tax assets are correct.

VI. Auditor's conclusions

- (a) The Company has presented the required information, reliable explanations and statements in due scope and time sufficient to conduct this audit, and has filed a statement confirming completeness of all data presented in accounting books and all contingent payables, as well as presentation all major post balance sheet events occurring after the date the statement was submitted.
- (b) The company keeps relevant documentation setting out the adopted accounting principles, which have been considered correct. Operations audited by the certified auditor were duly documented (documentary evidence being correct and transparent), and have been duly posted in the books in a proper way. Accounting entries subject to the audit are correct and accurate and based on accounting documentary evidence. The financial statement has been based on accurate accounting books.
- (c) Adopted accounting principles are used consistently. The closing balance as at the end of the previous reporting period has been correctly posted in the books as the opening balance for the current period.
- (d) Accounting books are kept based on a computer programme in a reliable, accurate and auditable manner. Protection of the access to data and data processing system is sufficient. Accounting documentation, books and financial statements are kept appropriately.
- (e) Based on the audit of reliability of individual items in the financial statement, the conclusion may be made that the internal control system ensures correctness and reliability of the accounting books.
- (f) Share capital was paid for pursuant to the law and has been found to exist.
- (g) Stock take conducted during the audited period was correct and pursuant to the provisions of the Accounting Act. Results of stock-take have been correctly calculated and posted in the accounting books.
- (h) Presentation of items influencing the gross financial result of the Company's operations in all its material aspects is complete and accurate.
- (i) The gross financial result has been appropriately translated into net financial result in all its material aspects.
- (j) The statement of changes in shareholders' equity and the cash flow statement have been duly presented in all their material aspects in relation to the balance sheet, profit and loss account and the accounting books.
- (k) Introduction and Notes to the financial statement include all material information required by the Accounting Act and present a true and fair view in all important aspects.

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- (l) The report on the Company's business is complete under provisions of the Accounting Act and the information presented therein is in line with the financial statement for the current period.
- (m) All figures presented in the Notes to the financial statement, supplemented with information included in chapters IV and V of the report, are in line with the certified auditors' professional standards issued by the National Council of Auditors in Poland (in all their material aspects).
- (n) It is hereby confirmed that both the entity entitled to conduct audits and the certified auditor are independent of the audited Company.