

**NETAŞ TELEKOMÜNİKASYON A.Ş. AND ITS' SUBSIDIARIES**

**BOARD OF DIRECTORS ACTIVITIES REPORT**

**FOR THE PERIOD ENDED 30 JUNE 2015**

Trade Registration Number: 94955/403045

**Headquarters**

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**ORGANIZATION AND OPERATIONS OF THE GROUP**

Netaş Telekomünikasyon A.Ş. and its' subsidiaries (The "Group") is an incorporated company, registered in İstanbul. The Group is engaged in the manufacture and trade of telecommunication equipment, project installation services, technical support, repair and maintenance services, IT services, strategic outsourcing services, implementation activities, and integration services. The shares of the Company are quoted on the Borsa İstanbul. The headquarters address has been registered as Yenişehir Mah. Osmanlı Bulvarı No:11 34912 Kurtköy-Pendik/İstanbul at İstanbul Trade Registry Office as at 23 July 2013.

The related to joint ventures and association of the Company is as follows:

• Probil

From industrial solutions to business solutions and from systems integration and outsourcing to care and maintenance services, network solutions and consultancy, Probil has been providing a wide range of services in international markets since 1989. Global competition is constantly increasing. Companies now begin to operate on a service- and customer oriented basis rather than simply focusing on products. This mandates companies to closely follow and use IT technologies more effectively. The Company has 100% shares of Probil.

• BDH

BDH offers brand-independent consultancy, strategic outsourcing, hardware and support services in the IT sector to a wide range of customers including small-scaled companies and larger enterprises and public institutions. With a service team of experienced and certified professionals specializing in different areas of IT, BDH provides with 36 branches and 46 partners to its customers throughout Turkey. BDH. Centers located in İstanbul, Ankara, İzmir, Bursa and Samsun offer hardware support for all kinds of IT products including servers, storage units, handheld devices, printers and more. The Company has indirectly 100% shares of BDH.

• Netaş Telecom LLP

Founded in Almaty, Kazakhstan, in 2012, Netaş Telecom LLP operates in line with Netaş's vision "To Become the Regional Systems Integrator". Netaş Telecom LLP is fully owned by the Company.

• Netaş Telecommunication Malta

"Netaş Telecommunications Malta Ltd" with an initial capital of only 1,200 Euros, this fully-owned subsidiary was established in Malta on 4 November 2014 for the purpose of improving operational effectiveness. Netaş Telecommunication Malta is fully owned by the Company.

• Kron

Kron Telekomünikasyon Hizmetleri A.Ş. produces software solutions for national and regional telecoms operators and service providers. The Company acquired the company's Group A shares in 2013 in line with its strategic growth goal and for the purpose of offering innovative solutions to its customers. Having strengthened its systems integration capabilities by acquiring Kron, the Company now provides a wider range of end to-end solutions to its customers in Turkey and the region. The Company has 10% shares of Kron.

The Group helps companies and institutions increase their productivity by providing service providers and institutions with end-to-end value added solutions, systems integration services and technology services in national and international markets through innovative and creative information technologies solutions.

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The Group provides its customers with new generation solutions in various areas such as network, security, unified communications, virtualization, cloud computing, broadband access, defense technologies, optic and carrier Ethernet, GSM-R, IT integration, strategic outsourcing and original software development.

The Group also plays an important role in the modernization of the defense communications network needed by the Turkish Armed Forces. As the lead systems integrator of Turkey, the Group carries out our activities with the power of our R&D department, which has strong insight about new generation technologies.

The Group acts upon the vision of working under global standards and becoming the number one systems integrators of Turkey and the region. The Group conducts strategic partnerships with global technology giants in order to help its customers closely follow developments in the information technologies business and to more effectively use technology. The Group's strategic partners include some of the best in class companies such as Cisco, Microsoft, Avaya, HP, Oracle, Genband, Kapsch and Wesley Clover. In addition to being the lead software exporter, the Group also develops software solutions for more than 200 global operators.

The Group provides services to more than 1,500 customers from the leading global telecom operators, to international companies in the enterprise market, leading banks and insurance companies, public institutions, including ministries and universities, energy and health businesses, defense and other industries. The Group is always investing in technology and innovation and delivers large integration projects. The Group offers solutions to institutions particularly in Asia-Pacific countries, Commonwealth of Independent States and North Africa. The Group focused on high-volume multi-technology projects in Turkey and abroad throughout 2015.

**SHAREHOLDER STRUCTURE:**

Shareholder structure of the Company as at 30 June 2015 and 31 December 2014 is as follows:

	<b>Share %</b>	<b>Share %</b>		
	<b>30 June 2015</b>	<b>31 December 2014</b>	<b>30 June 2015</b>	<b>31 December 2014</b>
OEP (*)	48,04	48,59	31.162.570	31.517.570
TSKGV (**)	15,00	15,00	9.729.720	9.729.720
Public	36,96	36,41	23.972.510	23.617.510
<b>Total</b>	<b>100</b>	<b>100</b>	<b>64.864.800</b>	<b>64.864.800</b>

(\*) OEP Turkey Tech B.V.

(\*\*) Turkish Armed Forces Foundation

As at 30 June 2015, total shares of OEP Turkey Tech B.V. in the Company is 48,04 % including 23.351.328,00 A-type and 7.811.242 B-type.

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**BOARD OF DIRECTORS**

The Members of Board of Directors as of 30 June 2015 are as follows:

Chairperson:	David Arthur Walsh
Vice-Chairperson:	M. Cumhuri Özdemiř
Member:	Joseph Patrick Huffsmith
Member:	Memet Yazıcı
Member:	Andrew Glover Dunn
Member:	Alpaslan Korkmaz (Independent)
Member:	Emre Şehsuvarođlu (Independent)

**THE GROUP'S MANAGEMENT:**

C. Müjdat Altay	Chief Executive Officer
M. İlker Çalıřkan	Chief Financial Officer
Yasemin Akad	Chief People Officer
Selcan Tařkıran	Chief Marketing Officer
Kamil Orman	General Manager -Defense Sytems and Public Sales
Ali İhsan Kuralkan	General Manager -International Sales
M.Ali Tombalak	General Manager -Enterprise Sales
Ahmet Hamdi Atalay	General Manager-Probil (Till 10 August 2015)
Osman Nuri Ertürk	General Manager-BDH
Gönül Kamalı	Research and Development Leader-Carrier Networking
Ömer Aydın	Research and Development Leader-Defense Systems
Öner Tekin	Research and Development Leader-Information Technology

**VISION, CORE VALUES, QUALITY POLICY**

**Vision**

Becoming Turkey's and Region's number 1 systems integrator working as per global standards.

**Core Values**

- Customers are our driving force.
- People are our strength.
- Quality is in every aspect.
- Innovation fuels our future.
- Accountability and integrity underpin everything.

# **NETAŞ TELEKOMÜNİKASYON A.Ş. AND ITS' SUBSIDIARIES ACTIVITIES REPORT OF THE BOARD OF DIRECTORS FOR THE PERIOD ENDED 30 JUNE 2015**

## **Quality Policy**

To constantly improve and ensure the sustainability of the Group's data-based quality management system established in compliance with international standards and aimed at achieving "Excellence" in order to create maximum value for its customers in line with the Group vision.

It is the responsibility of all Group employees to achieve "Excellence" through constant improvement.

## **R&D PROJECTS**

The Group operates with the support of R&D Center that employs 700 people, who have a deep insight on new generation technologies. Having acquired the "R&D Center" status in 2008 pursuant to Law 5746 on Supporting Research and Development Activities, the Group has been given many awards and has become the lead software exporter 4 times in the last 8 years in line with the "National Goal of Making Turkey a Regional Center for Medium and High Technology and Creating a Global Brand from Turkey".

Netaş, the oldest and the biggest private telecom R&D of Turkey, has been chosen the most successful R&D center for 2012 and 2013 in the performance evaluation of Science, Industry and Technology Ministry between the ongoing R&D centers for at least 2 years.

Knowing the importance of a strong R&D Center, we focus on the following 6 key topics for the purpose of expanding and strengthening the scope of the R&D ecosystem:

- Innovation and New Products
- International Relations and Cooperation
- Academic Relations and Cooperation
- Number of Patents, National and International Statements and Publications
- Training Qualified Personnel
- Cooperating with Technology Entrepreneurs

The Group switched to a faster and more effective business model in 2014 in order to make better use of R&D and innovation. This model is based on the "Business Unit" model, which is innovative, proactive and capable of meeting the needs of the future. Research and Development has turned into a business unit under the name of "Technology and Innovation Directorate" and the Company CEO Mr. Müjdat Altay has assumed the role of General Manager of the unit.

The most important goal of the Technology and Innovation Directorate is making innovation a corporate culture and enriching their product portfolio by adding high-technology value added products that would compete globally. For this purpose, the Group has organized various innovation events such as "Focus Innovation/Hackathon" and carried out activities under the "New Product Process".

The Group focuses on innovative and creative solutions in national and international markets in order to provide service providers and enterprises with network, unified communications, virtualization, cloud computing, defense technologies, public security, broadband mobile access, optic and carrier Ethernet, GSM-R, systems integration and technology services. The Group has provided more than 200 global operators with the software solutions that the Group developed in their own R&D laboratories. These solutions have helped the Group reaches a software export figure of USD 400 million in the last 10 years.

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The Group has started projects such as “4G LTE Advanced Base Station” design, a first in Turkey and “VoIP Security Tool” and “Media Security Platform - MSP”, the first members of a cyber security suite equipped with groundbreaking new features. Currently, its portfolio includes a total of 41 ongoing projects.

The Group has been strengthening and continuing the R&D relations established with multinational companies such as Genband, Kapsch, Ciena and Microsoft and developing products that would interoperate with the products of global giants such as Cisco and Avaya.

The Company uses the “open innovation” approach and aims to strengthen its relations with universities with the purpose of gaining a competitive edge and producing projects that compete globally.

In addition to its own R&D Center, our Group is also open to external ideas. Instead of using their own resources in everything, the Group prefers reaching the source of ideas, information and experience, making cooperation a win-win situation.

The unit of TUBITAK concerned with these affairs agreed to the Group’s application to contact and cooperate with entrepreneurs, who have a certain level of maturity in their projects and communicated the necessary announcements within the scope of this study. 10 of the responding entrepreneurs were interviewed and 6 of them were qualified as capable of conducting joint projects with the company. Their works were found suitable for integration into Netaş products. After that, detailed activities were started. Considering this effort of the Group as a successful example, TUBITAK plans to share and extend this initiative to other big companies.

Another “open innovation” activity for supporting technology entrepreneurship is to support young entrepreneurs in developing value added projects and encourage them to establish their technology companies by using the internationally-acknowledged original business model of the Netaş Wesley Clover Technology Fund. We have been successfully implementing these activities. The Netaş Wesley Clover Technology Fund receives the strong and continuous support of both the Group and Wesley Clover in terms of technology and consultancy.

The fund consists of four companies with the fifth being established. Three of these companies operate with four people and one with three people. These companies operate in the fields of IoT (Internet of Things), crowd sourcing, cloud-based form design for mobile field components, mobile software for collecting feedback from end users for quality improvement purposes and “venue management and indoor navigation”.

With the purpose of offering value added innovative products globally, the Group uses patents and brand protections measures in order to protect their working or planned ideas and strengthens our corporate value by adding ideas that are not directly related to their business. As at July 2015, national patent application increased by 20 and reached to 94 from 75 since the end of 2014. There are also 4 international patent applications.

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**GOVERNMENT GRANTS**

The Group is qualified for the incentives and exemptions provided by Support of Research and Development Act, numbered 5746 effective from 24 November 2008. As at 30 June 2015, the Group has a corporate tax benefit of 112 million TL, due to research and development spending of which 19 million TL is utilized (As at 31 December 2014, the benefits arising from 2014 was 81 million TL, of which 1 million TL was utilised).

For the period ended 30 June 2015, the amount of income tax incentive within the scope of Act numbered 5746 is 5 million TL (For the period ended 30 June 2014: 2 million TL) and the total amount of social premium incentive within the scope of Act numbered 5746 and Social Security and General Health Insurance Act numbered 5510 is 4 million TL (For the period ended 30 June 2014: 2 million TL).

For the period ended 30 June 2015 the Group has received 4 million TL cash incentive from TÜBİTAK for its research and development activities (For the period ended 30 June 2014: 2 million).

**DONATIONS MADE DURING THE PERIOD**

The Group does not have any donations in the first quarter of 2015.

**REMUNERATION PROVIDED FOR BOARD OF DIRECTORS**

Total remuneration provided for the board of directors for the period ended 30 June 2015 is 0,3 million TL. It was 0,2 million TL for the period ended 30 June 2014 for the board of auditors and board of auditors of the Group.

**RENUMERATION PROVIDED FOR TOP MANAGEMENT**

For the period ended 30 June 2015, and 2014, total remuneration provided for the Group Executive Management is 6 million TL and 5 million TL, consecutively.

No loans were extended to board of directors and board of auditors as at 30 June 2015 and 2014. The Group pays Executive Management bonuses and premiums on top of their salaries.

**FINANCIAL PERFORMANCE**

**a) Orders**

Order booked for the first half of 2015 is 580 million TL by 21% increase year over year (30 June 2014:478 million TL). Orders on hand as at 30 June 2015 is 785 million TL by 68% increase.

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**b) Income Statement Analysis**

The Group's export increases from 49 million TL to 64 million TL (increase by 31% year over year) for the first half of 2015.

The Group increased gross profit by 7% from 29 million TL to 31 million TL for the period ended 30 June 2015. The gross margin of the group is 9% (30 June 2014: 9%).

Net profit for the period ended 30 June 2015, increased by 6 million TL and reached to 3 million TL.

	<b>Q2'2015</b>	<b>Q2'2014</b>	<b>Change %</b>
Revenue	336	340	-1%
Cost of sales	(305)	(311)	-2%
<b>Gross profit</b>	<b>31</b>	<b>29</b>	<b>7%</b>
<i>Gross margin%</i>	9%	9%	100bps
Sales & marketing expenses	(22)	(19)	17%
General administrative expenses	(11)	(9)	19%
Research and development expenses	(1)	(1)	7%
Incentives	3	2	32%
<b>EBIT</b>	<b>1</b>	<b>3</b>	<b>-67%</b>
<i>EBIT margin %</i>	0%	1%	100bps
Depreciation	9	8	23%
<b>EBITDA</b>	<b>10</b>	<b>11</b>	<b>-4%</b>
<i>EBITDA margin %</i>	3%	3%	100bps

*\*EBIT = Gross Margin – Sales and Marketing Expenses – General and Administrative Expenses – Research and Development Expenses+ R&D Incentives*

*R&D Incentives: Disclosed under Income from Operations in the financial statements prepared in accordance with the Capital Markets Board requirements.*

*\*\* Operating Expenses= Sales and Marketing Expenses + General and Administrative Expenses + Research and Development Expenses- R&D Incentives*

*\*\*\*EBITDA= EBIT + Depreciation*

**c) Balance Sheet Analysis**

Net working capital requirement of the Group is 371 million TL as at 30 June 2015. Net working capital of the Group increased by 32 million TL compared to that of 31 December 2014. Net debt decreased by 11 million TL and was 120 million TL as at 30 June 2015.

The Group does not make a provision against the pre-filing receivables of 46 million TL from Nortel Group companies because it is not able to estimate the recoverability due to uncertainties as at the balance sheet date note 7.

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**d) Cash Flow Analysis**

	<b>Q2'2015</b>	<b>Q2'2014</b>	<b>Change %</b>
Net profit for the period	3	(3)	-191%
Adjustments to net profit for the period	9	19	-53%
Change in net working capital	(32)	13	-351%
Taxes paid	(2)	(2)	-11%
Payment for employee premiums, unused vacation accruals, retirement benefits	(14)	(15)	-3%
<b>Cash flows from operating activities</b>	<b>(36)</b>	<b>12</b>	<b>-415%</b>
Cash flows from investing activities	(5)	(2)	91%
Cash flows from financing activities	140	(4)	-4072%
Effects of exchange rate changes on cash and cash equivalents	(4)	(3)	26%
<b>Net increase/(decrease) in cash and cash equivalents</b>	<b>95</b>	<b>2</b>	<b>3841%</b>
<b>Cash and cash equivalents at the beginning of the period</b>	<b>84</b>	<b>41</b>	<b>106%</b>
<b>Cash and cash equivalents at the end of the period</b>	<b>179</b>	<b>43</b>	<b>315%</b>

The Group showed a great achievement in the collection of its trade receivables and increased the cash balance to 179 million TL from 84 million TL of the year beginning.

No dividend payment was made during the reporting period.

**e)Investor Information**

**Information on the share**

<b>Registration date:</b>	03.03.1967
<b>Number of shares:</b>	6.486.400 shares between 01.01.2012-06.08.2012; 64.864.000 shares between 06.08.2012-31.12.2012
<b>Initial public offering date:</b>	15.03.1993
<b>Percentage of publicly open shares:</b>	36,96%

The Company shares are traded at XU100 index since the beginning of the fiscal year 2014.

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**Earnings per share**

Earnings per share is 0,0478 TL for the second quarter of 2015 and the loss per share is 0,0527 TL for the same period of 2014.

It was approved by the Board of Directors on 13 April 2015 that there will be no dividend distribution in 2015. It has been submitted for the approval of the Annual General Assembly of the Company.

The closing share price in Istanbul Stock Exchange was 8,55 TL as at 30 June 2015. (31 December 2014: 6,67 TL) The market capitalization of the Company which was 433 million TL as of 31 December 2014 increased by 28% up to 555 million TL as at 30 June 2015.

**RISK MANAGEMENT**

**a) Credit risk**

The Group's credit risk is primarily dependent upon its trade receivables and exposures to the banks. The amounts presented in the balance sheet are net of allowances for doubtful receivables, (except for the amounts due from Nortel companies prior to 14 January 2009, where the Group has not made a provision against the pre-filing receivables from Nortel as the Group is not able to estimate the recoverability due to uncertainties as at the balance sheet date - see note 7 in the Financial Statements) estimated by the Group's management based on prior experience and the current economic environment.

Doubtful receivables are 4 % of the total receivables of the Group. The management of the Group does not foresee any other uncertainty on the receivables.

The Group assigns credit limits to its customer and exposures to the customers do not exceed these limits. The Group has significant exposures to the banks. The Group also assigns credit limits to the banks. Treasury and Control department monitors and controls exposures to the banks in order to ensure that the exposures are within the assigned limits.

**b) Liquidity risk**

The Group maintains its cash position in liquid assets and significant amount of liquid assets are kept in US Dollar as US Dollar has significant impact on the Group's operation. The Group is aiming to hold adequate resources to be able to fulfill its current and future liabilities.

**c) Foreign currency risk**

The Group's foreign currency risk is mainly associated with changes in the value of US Dollar against TL and other currencies. In order to avoid possible losses due to fluctuations of foreign exchange rates, the Group places its assets with the same currency for liabilities.

**d) Interest rate risk**

Interest rate-sensitive financial assets are placed in short term instruments in order to avoid any possible interest rate fluctuations. Interest rate-sensitive liabilities constitute 42% of the total liabilities.

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**2015 OUTLOOK**

The Group's objectives for 2015 include extending the portfolio of value added solutions and services to increase the efficiency of current and new customers and focusing more on vertical industry solutions. Another objective is to become the number one system integrator of the country and the near region by developing innovative products in its R&D laboratories in accordance with global new generation information technologies and large-scale complex technology projects, including products from multiple manufacturers.

Group financial objectives for 2015 include controlled growth and decreasing net capitalization requirements by increasing EBITDA.

In this sense, the Group does not estimate a significant increase in orders placed during 2015 but nevertheless intends to increase sales revenue by 8% (estimation in the activity report for the year ended 31 March 2015: %15) on a USD basis while improving EBITDA margin by 150 basis points (estimation in the activity report for the year ended 31 Mart 2015: 150 basis points). A significant annual change in the gross profit margin is not expected.

However, operational costs are expected to decrease by 10% annually on a USD basis. In this sense, the organizational change in the third quarter of 2014 will be most effective regarding the targeted improvement in operational costs.

Certain measures which had been planned during 2014 to be implemented by the end of 2015 to reduce the net capitalization requirement and, as a result, decrease net debt (total financial debts less cash available), intend to close 2015 with a positive net cash position.