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Independent Reasonable Assurance Report

To the Management and Supervisory Board of PLAVA LAGUNA j.s.c.

This report is produced in accordance with the terms of our contract dated 17 May 2017 for the purpose of reporting on the share/business interest exchange ratio in the process of the merger of the company ISTRATURIST UMAG j.s.c. (the merged company) with the company PLAVA LAGUNA j.s.c. (the acquiring company).

Definition of the subject matter and identification of the criteria

We have been engaged to perform an independent assurance engagement as to whether the share/business interest exchange ratio and applied valuation method is compliant, in all material respects, with the requirements set out in Articles 513 and 514 of the Croatian Company Act.

Management Boards' responsibility

The Management Boards of the merging companies, PLAVA LAGUNA j.s.c. (as the acquiring company) and ISTRATURIST UMAG j.s.c. (as the merged company), are responsible for determining the share/business interest exchange ratio. In addition, the Management Boards shall prepare a Merger Report in accordance with the criteria set out in Articles 513 and 514 of the Croatian Company Act. The Management Boards of the merging companies are responsible for presenting in a complete and accurate manner the information in the Merger Report that includes analyses of the following: the terms of Merger Agreement, share/business interest exchange ratio from a legal and economic perspective as well as the benchmarks used for the valuation of the companies as the basis for the share/business interest exchange ratio.

Our responsibility

Our responsibility is to report, based on our work, whether the share/business interest exchange ratio determined in the Merger Agreement and applied valuation method as presented in the Merger Report as compliant, in all material respects, with the requirements set out in Articles 513 and 514 of the Croatian Company Act.

We conducted our engagement in accordance with the International Standard on Assurance Engagements 3000 'Assurance Engagements other than Audits or Reviews of Historical Financial Information'. This standard requires that we comply with ethical requirements and plan and perform the assurance engagement to obtain reasonable assurance whether the share/business interest exchange ratio and applied valuation method as presented in the Merger Report is compliant, in all material respects, with the requirements of Articles 513 and 514 of the Croatian Company Act.

Our Independence and Quality Control

We have complied with the independence and other ethical requirements of the Code of Ethics for Professional Accountants issued by the International Ethics Standards Board for Accountants, which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

Our firm applies International Standard on Quality Control 1 and accordingly maintains a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

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Summary of the work performed

Within the scope of our work we performed, among others, the following procedures:

- Acquiring an understanding of the merger process, the reasons and objectives to be achieved by this business combination;
- Discussions with the staff entrusted with compiling and preparing the Merger Agreement and Merger Report;
- Comparing information presented in the Merger Report as of 29 June 2017 with the registration data on the incorporation of the merging companies;
- Understanding of the applied valuation methods used for determination the share/business interest exchange ratio, as stated in the Merger Report;
- Understanding of the calculation and verification of the mathematical accuracy of the share/business interest exchange ratio;
- Analysis of other valuation methods that may be used and reasons for not using them.

The analysis of the applied share exchange ratio methods and the reasons for their application are described in Appendix 1 to this report, as required by Article 515 (3).

We emphasise that the precondition for the merger procedure to be performed on the basis of determined share/business interest exchange ratio is the performance of the corporative measure involving split of shares of the company PLAVA LAGUNA j.s.c. by splitting each ordinary share without nominal value named PLAG-R-A to 4 ordinary shares (in 1:4 ratio).

The nature and extent of our procedures were determined based on our risk assessment and our professional judgment in order to obtain reasonable assurance.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our reasonable assurance opinion.

Reasonable assurance opinion

In our opinion, the share/business interest exchange ratio presented in the Merger Agreement and the applied valuation method presented in the Merger Report are compliant, in all material respects, with the requirements set out in Articles 513 and 514 of the Croatian Company Act.

Inherent limitation

Without modifying our opinion, we draw attention to the fact that this report is a reasonable assurance report and is not intended to, and does not, constitute a legal opinion on compliance with Articles 513 and 514 of the Croatian Company Act or other legislation.

PricewaterhouseCoopers d.o.o.
Zagreb, 29 June 2017

This version of our report is a translation of the original, which was prepared in Croatian language. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation

Appendix 1

Introduction

Based on the decision of the Commercial Court in Pazin ref.no. 10 R1-29/17-4 of 9 May 2017 on the appointment of the auditing company PricewaterhouseCoopers Ltd. Zagreb as auditor in the procedure of the merger of ISTRATURIST UMAG j.s.c. (hereinafter: merged company) with PLAVA LAGUNA j.s.c. (acquiring company), we conducted an audit of the merger of the two afore mentioned companies.

In accordance with the decision of the Commercial Court, the auditor shall, for each company participating in merger, review the Merger Agreement and prepare a written report on merger audit which will include the conclusion about the appropriateness of the proposed share exchange ratio and state the following:

1. the methods of establishing the share exchange ratio
2. the reasons for which the selected share exchange ratio method is appropriate
3. which share exchange ratio could be obtained from the application of different methods, if used, and the significance of individual methods for establishing the proposed exchange ratio and the value of on which it rests, and the specific difficulties that have arisen in assessing the companies.

Basic information about the companies participating in merger

a) Plava laguna j.s.c. (acquiring company) with its headquarters in Poreč, Rade Končara 12, (MBS 040020834;OIB 57444289760), formed as a joint stock company in accordance with the Companies Act and registered in the Court Register with the Commercial Court in Pazin. Major shareholder of the Company is Sutivan Investments Anstalt from Liechtenstein (Lukšić Group) with a share of 80.34% in total number of ordinary shares, and 100% ownership over preferred shares. The share capital of the company amounts to HRK 1,385,151,471.47, divided into 546,318 ordinary shares without nominal value, and 105,000 preferred shares of HRK 1,000 in nominal value. Company's shares are listed on the Regular market of listed instruments of the Zagreb Stock Exchange.

b) Istraturist Umag j.s.c. (merged company) with its headquarters in Umag, Jadranska 66, (MBS 040002769;OIB 22738374612), formed as a joint stock company in accordane with the Companies Act and registered in the Court Register with the Commercial Court in Pazin. Major shareholder of the company is Plava laguna j.s.c.. The share capital of the company amounts to HRK 467,499,500.00 and is divided into 4.674.995 ordinary shares of nominal value HRK 100.00 each, shares marked as ISTT-R-A. Company's shares are not listed on the Zagreb Stock Exchange.

Summary of legal aspects and the Merger Agreement

- Based on the decisions by the Boards of Managers of companies from 26th and 28th of April, 2017 and the approval by the Supervisory Boards from 27th and 28th of April, 2017, the merger procedure of the above mentioned companies has been initiated;
- For the purpose of the implementation of merger, it is necessary for the acquiring company top increase the share capital by issuing 12,500 new ordinary shares in the amount of HRK 7,618,681.88. Shareholders of the merged company will receive in the exchange for their shares marked as ISTT-R-A the shares of the acquiring company marked as PLAG-R-A, which will be given out of own ordinary shares held by the acquiring company and the newly issued ordinary shares of the same class;
- Shareholders of the merged company become shareholders of the acquiring company at the moment of the exchange of shares of the merged company they are holding with the shares of the acquiring company, in accordance with the established share replacement ratio;

- In order to respect the established exchange and provisions of Article 520, paragraph 4, of the Companies Act, given that the exchange ratio of the shares in the merged company for the shares in the acquiring company is such that it does not allow for one or more shares of the merged company to be replaced for the whole number of shares of the acquiring company, the acquiring company shall, to those shareholders in the merged company who do not hold a sufficient number of shares, pay the compensation in cash (but the total amount of compensations cannot exceed the one tenth of the share capital relating to given shares), as well as to respect the existing rights and shareholders' relations, prior to the merger, it is foreseen to divide every share in the acquiring company into 4 shares. Thus, without the increase of the share capital of the acquiring company, ordinary shares marked as PLAG-R-A are increasing in number from 546,318 to 2,185,272, and preferred shares marked as PLAG-P-A are increasing from 105,000 to 420,000, reducing the nominal amount of the shares from the first issue to HRK 250.00. At the same time, four shares give their holders the same rights as the existing one share.
- Upon registration of the merger in the Court Register of acquiring company, company ISTRATURIST UMAG, j.s.c. Umag ceases to exist and company PLAVA LAGUNA j.s.c. Poreč becomes its universal legal successor at which moment all assets and liabilities of the merged company are transferred to the acquiring company.

Valuations of companies for the purpose of determining the fair value per ordinary share

The valuations of companies, based on which the share exchange ratio is established, were conducted by an independent appraiser, company Deloitte Savjetodavne usluge Ltd. The procedure was conducted in a way that the assessments of value of companies Plava laguna j.s.c. and Istraturist Umag j.s.c. were done on an independent basis under the premise of value as a going concern in the existing legal form. The assessment of the company Jadranski luksuzni hoteli j.s.c. was also conducted for the purpose of determining the fair value of the share of 32.48% which Plava laguna j.s.c. owns in the mentioned company, besides 94.74% in the company Istraturist Umag j.s.c. The evaluation of all companies was carried out on a basis of financial statements as of 31 December 2016 as the date of the evaluation.

Applied methods for the determination of the share exchange ratio

The Boards of Managers of companies in the merger established the share exchange ratio on the basis of the discounted cash flow method (hereinafter: DCF method), while the market approach method (market multiple method) was used for supporting and validating the values obtained by the DCF method. These two methods were identified as most appropriate, given the intensive character of tourist activity in terms of capital on one side and high sensitivity (elasticity) of demand and revenues in this activity on the other side.

<u>The Discounted cash flow method (DCF)</u>

The usual practice on the capital market is that, due to shortcomings in the accounting value method, other methods for establishing the share exchange ratio for companies participating in merger are more often used, especially the Discounted cash flow method.

DCF method represents a dominant concept used for valuations in financial and economic practice, given that it is a dynamic method that results with the assessment of company's economic value based on the ability to generate future net cash flows. It is assumed that the most objective values for the purpose of determining the share exchange ratio, will derive from the valuation method based on the cash flows, which along with the application of an adequate discounted rate, i.e. the weighted average cost of capital (WACC), are reduced to present value.

In the transaction of companies merger, what becomes important for the investors is not only the change in capital structure but also the change in the ability of the ownership package for future periods. For shareholders or investors, this is especially manifested in the ability to increase capital and in the decision-making options in future business scenarios.

The DCF method gives the ability to the owner of the capital in a way that unites all future expenditures with future revenues and sources of future cash flows in a way to select and award the results to equity. The consistent application of such valuation method includes all future cash flows, based on whose gross presentation by discounting these values up to the date determined in the Merger Agreement the present value is recorded i.e. the present value of future flows is stated.

The main advantage of this method is that it can include all the pertinent future changes in the company. Surely, DCF method has its limitations, given that it is based on plans and prognosis of future results, realization of which may vary from set figures. However, the uncertainty that exists on the side of external influences acts in the same direction on all companies, given the same type of activity, with which this relative relation of the value assessment results in minimal changes.

Based on the stated reasons, it is clear that the DCF method is more acceptable compared to other valuation methods, especially in the activity of merging companies, because it can unite all the relevant driving values that affect the value of the company.

The Market multiple method

The market multiple method was used for comparison and validation of the value obtained by the DCF method, using the median and average of the MVIC (Market value of invested Capital) /EBITDA 2016 multiple for selected domicile companies in the same industry and comparable numbers measured by revenues, profit and accommodation capacity, and companies whose securities are listed on regulated capital markets. Greater applicability of the results of this method is with companies that reached a stable level of earnings that, according to the available information at the time of valuation, can be maintained in the future without further risk. However, the application of the aforementioned method within our framework involves a limitation in a form of very shallow market. Also, said method implies the static approach which uses historical data or past achievements.

The Comparable transactions method

The Comparable transactions method is finding comparable, similar transactions that have recently been concluded, and the application of relationships and ratios to a specific targeted case. Mentioned method was used by the Assessor to assess the value solely in the domain of tangible assets not in operation, based on the information on realized purchases and sales of properties that are similar, from the eNekretnine database.

Other methods not used for calculation of the share exchange ratio

In reviewing the share exchange ratio, the Boards of Managers also took into consideration the following method:

Carrying value method

Valuation by relying solely on the carrying value is also not applicable. Besides the fact that this method implies the static approach which also relies on the past data, the use of the stated values for the mentioned purpose is questionable. Namely, the precursors to the companies which participate in the transaction in question are socially-owned companies, which in the course of ownership transformation altered their legal structure into joint stock companies, and given the size of their tangible assets, the approach to establishing their values and valuation methods are probably different.

Besides methods reviewed by the Boards of Managers, we have taken into consideration some other valuation methods as well.

Comparative method

The comparative method is suitable for countries with an organised real estate market and where there is a credible database of sales transactions concluded. In concrete circumstances, this method has a significant disadvantage because there is no credible database in Croatia that could be used for comparable valuation of companies, and there are no information on valuations that could be used for comparison.

Liquidation method

The audited annual financial statements have not disclosed any circumstances which would indicate that there is a going concern issue and therefore, the liquidation method is not applicable.

Other methods

Valuation methods based on analysis of historical costs were not used as they are not appropriate for the activity in which the market awards non-material elements and seasonal events for which there is no cost of acquisition, such as: general tourist attractiveness, regional and world security crises, general informational and promotional activities, impressions and opinions that encourage general trends and spontaneous consumers, intentional and non-intentional influences in the region, changes in traffic situations, cultural events, phenomena of sacral and other objects, environmental effects and ecological incentives, substitution influences from other industries and similar.

Current market (average) or the last spot value is not appropriate for calculating any ratio of stock exchange due to very shallow market for these shares on the existing financial market, as well as due to the current general financial market problem.

Given that other reviewed valuation methods are not appropriate, no share exchange ratio has been calculated by these methods.