

# CITY INTERACTIVE GROUP

INTERIM MANAGEMENT REPORT  
FOR THE FIRST HALF OF 2012



Warszawa, August 30, 2012

## City Interactive S.A. Management Board Declaration

Pursuant to the Ordinance of the Minister of Finance of February 19, 2009 (Polish Journal of Laws no. 33, item 259 as amended) *on current and periodic information provided by the issuers of securities and the conditions for recognizing information required by the provisions of law of a non-member state as equivalent*, the Management Board of City Interactive S.A. declares that to the best of its knowledge the consolidated interim financial statements and comparative data have been drawn up in accordance with binding accounting principles, and correctly, reliably and clearly reflect the financial and property situation of the City Interactive Group together with its financial result, and that the interim management report of the City Interactive Group contains a true depiction of the development, achievements and situation of the City Interactive Group, including a description of principal threats and risks.

The Management Board of City Interactive S.A. declares that the entity authorized to audit financial statements performing audit of the consolidated interim financial statements was selected in accordance with the provisions of law and that such entity and the statutory auditors conducting the audit fulfilled the conditions for issue of an impartial and independent report on audit of the financial statements in accordance with the regulations and professional standards in force.

Management Board of City Interactive S.A.

**Marek Tymiński**  
President of the Management Board

**Andreas Jaeger**  
Member of the Management Board

Warsaw, August 30, 2012



## I. General characteristics of City Interactive Group operations

The City Interactive Group operates in the video game development and publishing market, both within Poland and abroad. The Issuer is the first publically traded company in this sector in Central and Eastern Europe and the first to become an international player, achieving outstanding market and financial performance. The City Interactive Group is focused on developing a high quality product range within different game genres, with a special focus on action games.

Within its business in the gaming market, the Parent appears as:

- Developer – having its own development studio in which new projects are created,
- Publisher – acquiring licenses to games manufactured by external studios, being responsible for marketing strategy and product roll-out,
- Distributor – which sells products directly to retail chains, distributor networks, internet portals and others.

Through fulfilling these three functions, the Issuer can effectively control the process of development and distribution of games without needing to involve a large number of other companies (agents) in the process of introducing its products to the market.

The City Interactive Group makes good use of its main assets: an experienced team, worldwide distribution network and cost advantage linked with lower profitability thresholds in relation to other, much larger developers. The Issuer's product range covers all price segments. Games developed for the Sony PlayStation®3, Xbox360® and PC have high commercial potential and are competitive in relation to others present in the market. The Group is also working intensively on supplementing the product range with games from new segments, including role-playing-games, titles for Android™ and iOS platforms and online games.

## II. Share capital

### 2.1. Share capital of the Parent – City Interactive S.A.

Share capital of City Interactive S.A. amounts to PLN 1 265 000 and is divided into 12 650 000 shares at a nominal value of PLN 0.10 each, of which:

- 10 000 000 series A shares,
- 40 000 series B shares,
- 2 500 000 series C shares,
- 110 000 series D shares.

Series A shares were acquired by then-current shareholders in City Interactive Sp. z o.o. at the moment the company was transformed into a spółka akcyjna (joint stock company).

Series B shares were issued under an incentive scheme and were acquired by City Interactive Group employees and associates. The District Court made registration of the increase in share capital under issue of series B shares on August 10, 2007.

Series C shares were subject to a successful public offering in November 2007. All offered shares on offer were purchased and paid for. On December 17, 2007 the District Court in Warsaw made registration of the increase in the Company's share capital through issue of series C shares.

Series D shares were issued under an incentive scheme and were acquired by Company employees and associates. The District Court made registration of the increase in share capital under issue of series D shares on October 9, 2009.

There are no securities carrying special control entitlements in relation to the Issuer, since in accordance with City Interactive S.A.'s articles of association all shares issued are ordinary

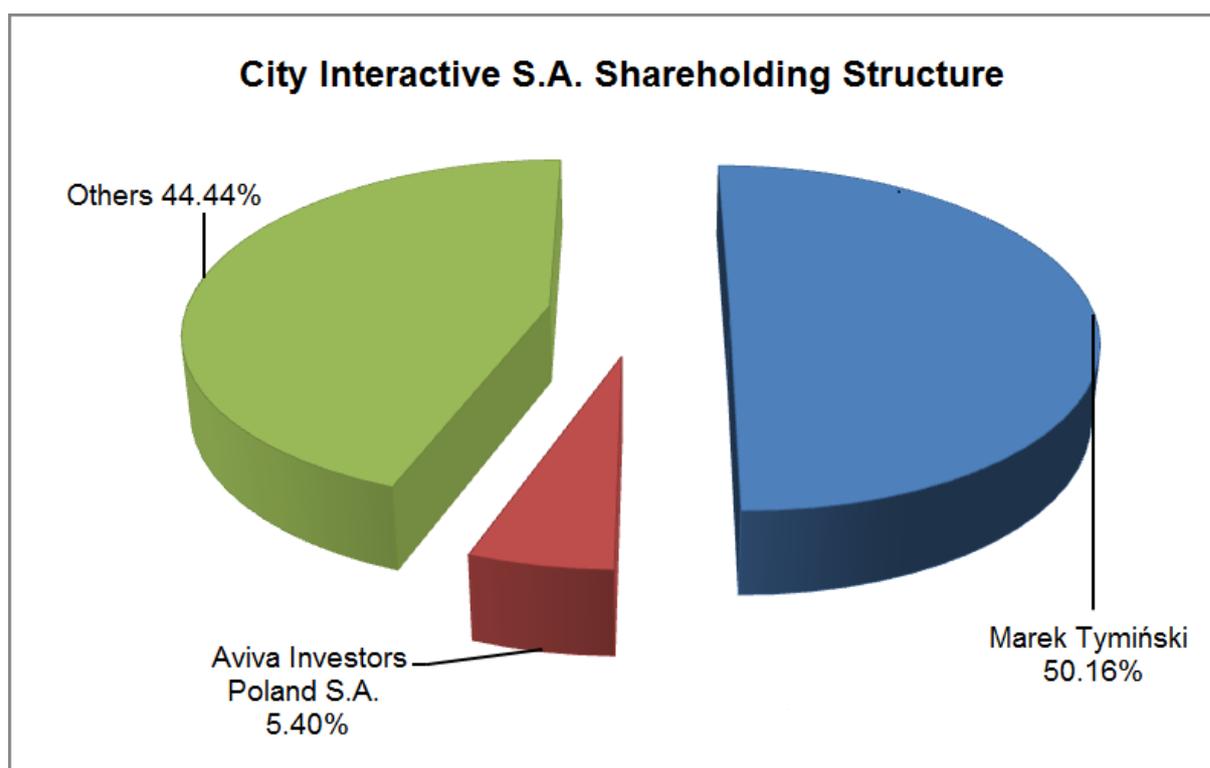
bearer shares with equal nominal value carrying the same rights and obligations for each shareholder.

**2.2 Indication of shareholders directly or indirectly through subsidiaries holding at least 5% of total votes at the Parent's General Meeting as at the date of publishing the quarterly report, with indication of the number of shares held by such entities, their percentage in share capital, the number of votes carried thereby and their percentage share in the total number of votes at the General Meeting, together with indication of changes in the ownership structure of significant blocks of the Issuer's shares during the period from publication of the previous quarterly report**

The total number of votes at the General Meeting of Parent City Interactive S.A. is 12 650 000.

**City Interactive S.A. shareholding structure as at the publication date of this report:**

Shareholder	number of shares	% in share capital	number of votes at GM	% of votes at GM
Marek Tymiński	6 345 794	50.16%	6 345 794	50.16%
Aviva Investors Poland S.A.	683 104	5.4%	683 104	5.4%
Non-controlling interests		44.44%		44.44%



During the period from publication of the Issuer's last quarterly report to date (i.e. between May 15, 2012 and August 30, 2012) the following changes in the Issuer's shareholding structure took place:

- on May 23, 2012 the company received notification from Marek Tymiński, President of the Management Board of City Interactive S.A., concerning his transfer on May 23, 2012 of 150 000 shares in City Interactive S.A. on the basis of a contract of donation executed on May 17, 2012. As at May 23, 2012 Marek Tymiński held 6 325 794

shares in the company, constituting 50.01% of total shares and carrying 50.01% of votes at the General meeting of Shareholders of City Interactive S.A.

- on July 27, 2012 the company received notification from Marek Tymiński, President of the Management Board of City Interactive S.A., concerning his acquisition on July 27, 2012 of 15 000. As at July 27, 2012 Marek Tymiński held 6 340 794 shares in the company, constituting 50.12% of total shares and carrying 50.12% of votes at the General meeting of Shareholders of City Interactive S.A.
- on July 31, 2012 the company received notification from Marek Tymiński, President of the Management Board of City Interactive S.A., concerning his acquisition on July 31, 2012 of 5 000. As at July 31, 2012 Marek Tymiński held 6 345 794 shares in the company, constituting 50.16% of total shares and carrying 50.16% of votes at the General meeting of Shareholders of City Interactive S.A.

**2.3. Presentation of shareholdings in City Interactive S.A. or right to shares by the Issuer's management or supervisory personnel as at the date of publishing the report, together with indication of change in shareholding during the period from publication of the previous quarterly report, presented individually for each person**

Person	Position	As at May 15, 2012	Increase in shareholding during the period from May 15, 2012 to August 30, 2012	Decrease in shareholding during the period from May 15, 2012 to August 30, 2012	As at August 30, 2012 (report publication date)
Marek Tymiński	President of the Management Board	6 475 794	20 000	150 000	6 345 794
Andreas Jaeger	Member of the Management Board	-	5 000	-	5 000
Lech Tymiński	Member of the Supervisory Board	9 565	-	-	9 565

**2.4. Information on agreements known to the Issuer, pursuant to which there may be a change in the proportions of shares held by current shareholders. Indication of limitations concerning transfer of ownership to securities in the Parent**

The Parent has no information concerning other agreements (including agreements entered into after the end of the reporting period) under which proportions of shares held by existing shareholders might change in the future. There are also no limitations on exercise of the right to vote carried by the Issuer's shares.

**2.5. Information on employee share program control system**

All shareholders whose stake in the Issuer's share capital as at the date of approving the issue prospectus exceeded 2% undertook towards the Parent that during the twelve-month period from the date of the first listing of rights to the Issuer's shares on the Warsaw Stock Exchange they would not encumber or pledge – with the exception of the possibility to establish a pledge for a bank in order to provide collateral for loans, nor dispose nor in any other manner transfer ownership, nor undertake to perform such action in relation to the entirety or part of shares, in any manner for the benefit of any person or entity unless consent for such action is expressed by the Parent's Supervisory Board. The obligation was intended to cease being binding in the event that City Interactive S.A.'s share price (closing rate on the WSE) exceeded the issue price by at least 20%. The above obligation concerned a total of 8 987 265 series A shares held by the above-mentioned shareholders, which



constituted 90% of shares held by them as at the date on which the prospectus was approved.

All shares which were subject to agreements on limitation of their assignability were deposited in brokerage accounts maintained by Dom Maklerski IDMSA.

In July 2007 the Parent issued 40 000 series B shares at an issue price of PLN 1 under a motivational program for its employees and significant associates. Persons subscribing for series B shares entered into a lock-up agreement with the Parent, limiting the assignability of shares for a period of either two or three years. In this manner the Issuer's employees and associates holding a total of 40 000 series B shares in City Interactive S.A., constituting in total 100% of series B shares in the Issuer, entered into an agreement with the Parent pursuant to which they undertook not to dispose of any of series B shares held for a period of 1 year and:

- 70% of series B shares held for a period of one subsequent year for a total of 20 150 shares,

- 90% of series B shares held for a period of one subsequent year for a total of 19 850 shares,

Furthermore some persons under the aforementioned motivational program also became the holders of series A shares at a price of PLN 1. Employees and associates holding a total of 35 650 series A shares in City Interactive S.A. submitted an official obligation not to dispose of any of the shares held for a period of 1 year and 90% of shares held for a period of two subsequent years.

All shares which were subject to agreements on limitation of their assignability were deposited in brokerage accounts maintained by Dom Maklerski IDMSA.

In the event of employment or cooperation being terminated with a shareholder holding shares covered by the motivational program, his/her shares were or are transferred to another person designated by the Company's Management Board.

110 000 ordinary series D shares in the Parent were issued on 30 June 2009. These shares were subscribed for by the Parent's employees at the issue price – PLN 1 per share.

There are also no limitations on exercise of the right to vote carried by the Issuer's shares subscribed for under the employee scheme.

### **III. Organizational structure of the Issuer's Group with indication of entities subject to consolidation**

Composition of the City Interactive Group as at June 30, 2012:

- **City Interactive S.A.**, having its registered office in Warsaw. Share capital of PLN 1 265 000. Group parent.
- **City Interactive Germany GmbH** – a company having its registered office in Frankfurt am Main, Germany. Share capital of EUR 25 000. 100% of shares held by City Interactive S.A. Company subject to consolidation as of the second quarter of 2008.
- **City Interactive USA Inc.** – a company having its registered office in Delaware, USA. Share capital USD 50 000. 100% of shares held by City Interactive S.A. Company subject to consolidation as of the second quarter of 2008.
- **Business Area Spółka z o.o.** – a company with registered office in Warsaw, subject to consolidation as of Q3 2010. Share capital of PLN 5 000. 100% interest held by City Interactive S.A.
- **City Interactive Studio S.R.L.** – a company having its registered office in Bucharest, Romania. 100% of shares held by City Interactive S.A. This company is subject to consolidation from Q4 2011.

- **City Interactive Canada Inc.** – a company based in Ontario, Canada, established in October 2010. Share capital of CAD 10.00. 100% of shares held by City Interactive S.A. The company is not subject to consolidation with regard to the fact that its financial results are not significant for assessment of the Issuer's situation.
- **City Interactive Studio Ltd.** – a company based in London, UK, established in December 2010. Share capital of GBP 100.00. 100% of shares held by City Interactive S.A. Company subject to consolidation from Q1 2011.
- **City Interactive UK, Ltd.** – a company having its registered office in Manchester, UK. Founding capital of GBP 100. 100% of shares held by City Interactive S.A. This company is not subject to consolidation with regard to the fact that its financial results are insignificant for assessment of the Issuer's situation.
- **City Interactive Spain S.L.** – company having its registered office in Madrid, Spain. Share capital of EUR 3 600. 100% of shares held by City Interactive S.A. The company is subject to consolidation as of the fourth quarter of 2008, whereas on January 1, 2010, after creation of revaluation write-offs on receivables, it was excluded from consolidation.

Furthermore, in 2008 the parent acquired shares in the following entities operating in South America and subsequently in 2009 opted out of their further development. These entities are currently not subject to consolidation with regard to discontinuation of their operations and the creation of provisions at parent level:

- City Interactive Peru SAC (formerly UCRONICS SAC) – a company having its registered office in Lima, Peru. 99% interest. Share capital of PEN 2 436 650. The company was subject to consolidation from the date of acquisition of a controlling block of shares to the end of 2008.
- City Interactive Jogos Electronicos LTDA – a company having its registered office in Sao Paulo, Brazil. Founding capital of BRL 100 000. 90% interest, remaining 10% held by City Interactive USA, Inc.
- City Interactive Mexico S.A. de C.V. – company having its registered office in Mexico City, Mexico. Founding capital of MXN 50 000. 95% interest, remaining 5% held by City Interactive USA, Inc.

After the end of the reporting period City Interactive S.A. sold 100% of shares in City Interactive Studio Ltd. to a non-related entity.

#### **IV. Description of the Group's significant achievements or set-backs in H1 2012 and events impacting its financial results**

- **Development of the *Sniper: Ghost Warrior* iOS mobile version moved to the Issuer's studio in Katowice, Poland**

On February 20, 2012 the Management Board of Business Area Sp. z o.o. withdrew from the production agreement with Vivid Games Sp. z o.o. The Issuer's Management decided that, through making use of the Group's production capacity, further work on the mobile version of *Sniper: Ghost Warrior* will be transferred to the Issuer's internal production studio in Katowice.

Mobile version of *Sniper: Ghost Warrior* on iOS platforms, i.e. the iPad®, iPhone® and iPod Touch®, will be produced based on Epic Games Inc.'s Unreal® Engine3 technology. The release is planned for August 21, 2012.

- **Execution of a significant agreement concerning sales of *Sniper: Ghost Warrior 2* and *Dogfight 1942* in Japan**

On February 23, 2012 a licensing agreement was entered into with Cyberfront Corporation, based in Tokyo, Japan, concerning sale of *Sniper: Ghost Warrior 2* on Sony Playstation®3, Xbox®360 and PC and sale of *Dogfight 1942* on Sony Playstation®3, Xbox®360 and PC.

- **Execution of a significant agreement concerning sales of *Sniper: Ghost Warrior 2* and *Dogfight 1942* in the UK, Italy, Spain and Greece**

On February 28, 2012 the Company executed a distribution agreement with Namco Bandai Partners S.A.S. concerning sales of *Sniper: Ghost Warrior 2* on Sony Playstation®3, Xbox360® and PC and sale of *Dogfight 1942* for Sony Playstation®3, Xbox360®, Nintendo Wii™ and PC in the UK, Italy, Spain and Greece.

- **Execution of a significant agreement concerning sales of *Sniper: Ghost Warrior 2* in Germany, Austria and Switzerland**

On April 27, 2012 the Company executed a distribution agreement with UBISOFT GmbH headquartered in Germany concerning sales of *Sniper: Ghost Warrior 2* for Sony Playstation®3, Xbox360®, Nintendo Wii™ and PC in Germany, Austria and Switzerland.

- **Changes in City Interactive S.A. management**

On March 14, 2012 Member of the Management Board Michał Sokolski resigned. Also on March 14, 2012 the City Interactive S.A. Supervisory Board Andreas Jaeger appointed as Member of the Management Board, serving as Finance and Operations Director.

- **Release of *Enemy Front* at the beginning of 2013. Additional content for *Sniper: Ghost Warrior 2***

On May 11, 2012 the Management Board of City Interactive S.A. announced its decision to reschedule the release of *Enemy Front* for PlayStation®3, Xbox360® and PC to the beginning of 2013. The Issuer's management took this decision in order to best ensure the highest product quality and to use personnel working on *Enemy Front* (at the Rzeszów studio) to create additional content for *Sniper: Ghost Warrior 2*, which will be published as DLC (downloadable content) immediately following the game's release. Also, the team at the Rzeszów studio (*Enemy Front*) may provide additional support for the development of *Sniper: Ghost Warrior 2* if necessary. The Issuer's management believes that the decision may contribute to maximizing both sales of *Sniper: Ghost Warrior 2* and *Enemy Front*. As at the publication date of this report, the release of *Enemy Front* is planned for H1 2013.

- ***Sniper: Ghost Warrior 2* global release date**

On July 25, 2012 the Management Board of City Interactive S.A. announced that the global release of *Sniper: Ghost Warrior 2* was scheduled for January 15, 2013. After subsequent detailed analysis of the progress of work on the project, the Issuer's management decided that, due to the need for additional work on the game's multiplayer version and optimization of *Sniper: Ghost Warrior 2* functionality for PlayStation®3, it was necessary to extend the project deadline. Considering the unfavorable competitive environment in November and December 2012 (a large number of releases in the genre being planned for the pre-holiday period), the Company's management selected January 15, 2013 as the optimal date for *Sniper: Ghost Warrior 2*'s worldwide launch on the Playstation®3, Xbox360® and PC

- **Resolutions of the General Meeting of City Interactive S.A.**

On June 28, 2012 the General Meeting of Shareholders approved the separate and consolidated financial statements and management report for the 2011 financial year. It also approved the Supervisory Board report for the same period and adopted a decision on allocation of the Company's 2011 net profit to a dividend fund. The General Meeting of Shareholders granted a vote of approval to members of the Management Board and Supervisory Board in respect of their duties in 2011.

## V. Selected financial data

Balance sheet data was converted according to the average exchange rate published by the National Bank of Poland as at the end of the reporting period:

- EURPLN as at December 31, 2011 – 4.4168
- EURPLN as at June 30, 2012 – 4.2613

Items in the statement of profit and loss and statement of cash flows according to the average exchange rate, calculated as the arithmetical average of exchange rates announced by the National Bank of Poland as at the last day of the month in a given period.

- Q1 2011 – 3.9742
- Q2 2011 – 3.9604
- Q1 2012 – 4.1750
- Q2 2012 – 4.2741

Selected financial data converted into EUR:

STATEMENT OF PROFIT AND LOSS	H1 2012		H1 2011	
	PLN thousands	EUR thousands	PLN thousands	EUR thousands
<b>Net revenue from sales</b>	<b>18 008</b>	<b>4 263</b>	<b>43 228</b>	<b>10 896</b>
Profit (loss) from operating activities	- 3 301	- 781	12 482	3 146
Gross profit (loss)	- 5 326	- 1 261	12 368	3 117
<b>Net profit (loss)</b>	<b>- 4 635</b>	<b>- 1 097</b>	<b>10 117</b>	<b>2 550</b>
Number of shares (in thousands)	12 650	12 650	12 650	12 650
Profit (loss) per ordinary share	- 0.37	- 0.09	0.80	0.20

STATEMENT OF PROFIT AND LOSS	Q2 2012		Q2 2011	
	PLN thousands	EUR thousands	PLN thousands	EUR thousands
<b>Net revenue from sales</b>	<b>8 369</b>	<b>1 958</b>	<b>29 847</b>	<b>7 536</b>
Profit (loss) from operating activities	- 2 512	- 588	10 956	2 766
Gross profit (loss)	- 3 196	- 748	10 829	2 734
<b>Net profit (loss)</b>	<b>- 2 587</b>	<b>- 605</b>	<b>8 985</b>	<b>2 269</b>
Number of shares (in thousands)	12 650	12 650	12 650	12 650
Profit (loss) per ordinary share	- 0.20	- 0.05	0.71	0.18

BALANCE SHEET	June 30, 2012		December 31, 2011	
	PLN thousands	EUR thousands	PLN thousands	EUR thousands
Non-current assets	42 772	10 037	28 779	6 516
Current assets	24 627	5 779	41 875	9 481
<b>Total assets</b>	<b>67 399</b>	<b>15 816</b>	<b>70 654</b>	<b>15 997</b>
Equity	54 341	12 752	57 772	13 080
Share capital	1 265	297	1 265	286
<b>Liabilities</b>	<b>13 057</b>	<b>3 064</b>	<b>12 882</b>	<b>2 917</b>
Non-current liabilities	264	62	342	77
Current liabilities	12 794	3 002	12 540	2 839
<b>Total equity and liabilities</b>	<b>67 399</b>	<b>15 816</b>	<b>70 654</b>	<b>15 997</b>

STATEMENT OF CASH FLOWS	H1 2012		H2 2011	
	PLN thousands	EUR thousands	PLN thousands	EUR thousands
Net cash flows from operating activities	7 393	1 750	10 751	2 710
Net cash flows from investing activities	- 15 465	- 3 661	- 7 163	- 1 806
Net cash flows from financing activities	- 15	- 4	- 5 224	- 1 317
<b>Net cash flows</b>	<b>- 8 087</b>	<b>- 1 914</b>	<b>- 1 637</b>	<b>- 413</b>

## VI. Description of atypical factors and events impacting on the operating results

In H1 2012, revenue from sales reached PLN 18 million. The lower-than-expected figure compared with the same period last year resulted primarily from a lack of new releases during the reporting period (whereas H1 2011 saw the release of *Sniper: Ghost Warrior* for Sony PlayStation®3) and decreased prices for *Sniper: Ghost Warrior* in most markets as a result of the typical computer game lifecycle. **Błąd! Nieprawidłowe łącze.**

Sales structure	H1 2012	Q2 2012	H1 2011	Q2 2011
Console games	91%	94%	92%	95%
PC games	9%	6%	8%	5%

Over the periods compared, North America increased its share within the Group's sales structure by geographical area, reaching 48% in the first half of 2012. North America's low share in H1 2011 (35%) resulted from the delayed North American release of *Sniper: Ghost Warrior* for Sony PlayStation®3 (June 28, 2011) compared to Europe (April 12, 2011).

Data in PLN thousands

Geographical structure	H1 2012		Q2 2012		H1 2011		Q2 2011	
	Revenues	% share	Revenues	% share	Revenues	% share	Revenues	% share
Europe	8 217	46%	3 695	44%	24 515	57%	17 465	58%
North America	8 709	48%	4 297	51%	15 239	35%	9 966	33%
Asia and Australia	1 082	6%	377	5%	3 474	8%	2 777	9%
<b>TOTAL</b>	<b>18 008</b>	<b>100%</b>	<b>8 369</b>	<b>100%</b>	<b>43 228</b>	<b>100%</b>	<b>30 208</b>	<b>100%</b>

The Group's margin, calculated as gross profit on sales over revenue from sales, reached 26% in H1 2012 (compared to 48% in H1 2011). This decrease between the periods results from successive reductions in the price of *Sniper: Ghost Warrior* across all platforms, while in the same period last year the Sony PlayStation®3 version was marketed at regular prices.

During the reporting period administrative expenses amounted to PLN 3.0 million, representing a 7% increase over 2011, attributable to the Group's development. Distribution costs in the periods compared decreased by 25% to PLN 4.1 million, resulting mainly from lower sales.

During the reporting period the City Interactive Group created impairment charges on inventory and prepayments for intangible assets totaling PLN 0.5 million. This resulted in an increase of other operating expenses compared to the same period last year.

The Group's net result generated during the reporting period was also significantly impacted by finance costs, which amounted to PLN 2.2 million. These were mainly due to unfavorable currency movements during the period compared to the higher currency levels at the end of 2011. Given the above, the Group realized negative exchange differences arising at the time of payment for foreign currency-denominated liabilities at a lower exchange rate than at the time of incurrence of these liabilities. Also, at the end of the reporting period the Group valued its liabilities in foreign currencies at a lower average exchange rate than on the

invoice dates. Finance costs were further impacted by valuation of forward contracts, described in point XVIII of this report.

As at June 30, 2012, the Group held PLN 8.6 million in bank accounts, down PLN 8.1 million from December 31, 2011. In the first half of 2012 the Group generated a PLN 7.4 million cash surplus from operating activities, while incurring expenditures of PLN 15.5 million, including PLN 14.1 million on financing new game development.

#### **VII. Explanations concerning the seasonal or cyclical nature of the City Interactive Group's business in the presented period**

Due to the variety of revenue streams (domestic distribution, international distribution, sale of licenses) and the specifics of the computer gaming industry, the City Interactive Group is subject to sales revenue volatility during the financial year, which is determined by the release of new products. The Issuer establishes the dates for release of its games in order to select the most beneficial competitive environment and in order for the release to achieve the highest financial result.

#### **VIII. Indication of proceedings in progress before a court, competent authority for arbitration proceedings or public administration authority**

The Issuer's Management has no information concerning any proceedings in progress against it or its subsidiaries the value of which (separately or jointly) exceeds 10% of the Issuer's equity.

#### **IX. Information on change in contingent liabilities or assets which occurred since the end of the last financial year**

As at June 30, 2012 the company had no contingent liabilities except promissory notes issued by City Interactive S.A. for lessor Raiffeisen Leasing Polska in order to secure payments under concluded leasing agreements.

#### **X. Information on grant by the Issuer or one of its subsidiaries of sureties for credits or loans or grant of guarantees – to an entity or subsidiary of such entity if the total value of existing sureties or guarantees constitutes the equivalent of at least 10% of the Company's equity**

During the period from January 1 to June 30, 2012, neither the Issuer nor any of its subsidiaries issued loan sureties or guarantees, the value of which could constitute at least 10% of the Issuer's equity.

#### **XI. Information concerning the issue, buy-back and repayment of equity and debt instruments**

During the reporting period, parent City Interactive S.A. did not issue, redeem or repay equity or non-equity instruments.

#### **XII. Indication of the effects of changes in the structure of the economic entity, including as a result of merging economic entities, acquisition or disposal of group entities, non-current investments, divisions, restructuring and discontinuation of activity**

During the reporting period there were no changes in the structure of the Group.

#### **XIII. Information on conclusion by the Issuer or one of its subsidiaries of one or more transactions with related entities, if these are individually or jointly significant**

**and have been executed on conditions other than market conditions, with indication of their values**

During the reporting period neither the parent nor its subsidiaries executed transactions which were atypical, exceeded the normal course of business with related entities or which were significant either individually or jointly.

**XIV. Information on distributed (or declared) dividend – total and per share, with division into ordinary and preferred shares**

During the reporting period the Parent City Interactive S.A. neither paid out or distributed a dividend.

**XV. Other information which the Company's Management believes is essential for assessment of its HR, property or financial situation, financial result and related changes, as well as information essential for assessing the ability of the Issuer's Group to satisfy its liabilities**

In the opinion of the Management of City Interactive S.A., no information other than that included in this report will appear which could be significant for assessing the Issuer's HR, property and financial situation (including financial result) or related changes and for assessing the Issuer's and its subsidiaries' ability to satisfy its obligations.

**XVI. Management's position concerning the possibility to meet previously published earnings forecasts for a given financial year in light of the results presented in the interim report in relation to forecast results**

On April 17, 2012 the Management Board of City Interactive S.A. announced that, in line with the Company's estimates, net consolidated revenue from sales generated by the City Interactive Group in the first quarter of 2012 exceeded PLN 11 million. On the date of publishing this report the Management Board of City Interactive S.A. announced an adjustment to the Group's initial estimated revenue from sales for Q1 2012, publishing a figure of PLN 9 638 000.

After consultation with the auditor it was confirmed that it is not possible to include the PLN 2 060 000 advance payment under the license agreement for sale of *Sniper: Ghost Warrior 2* on Sony Playstation®3, Xbox360® and PC from Cyberfront Corporation in Tokyo, Japan, in the Group's revenue. This was an adjustment on an accrual basis. The amount received constitutes 50% of the guaranteed, non-refundable advance payment; the revenue is certain and will be recognized in the statement of profit and loss in the third quarter of 2012, when the Issuer transfers the completed version of *Sniper: Ghost Warrior 2* (Gold Master) to Cyberfront Corporation.

On July 11, 2012 the Management Board of City Interactive S.A. announced that, according to the Company's preliminary estimates, consolidated net revenue from sales generated by the City Interactive Group in the second quarter of 2012 reached PLN 6.7 million. On July 26, 2012 the Management Board of City Interactive S.A. published a correction of the preliminary estimates for the Group's revenue from sales in Q2 2012, announcing that the figure was PLN 8 million. The reason for this correction was an increase in revenue from North American sales, which the Issuer became aware of after publishing the preliminary estimates.

In relation to the results presented in this interim report, the Issuer's Management has not published any estimates or forecasts concerning the City Interactive Group's consolidated revenues and results.

**XVII. Indication of events which occurred after the date of these interim financial statements, which were not recognized in the statements and which may have a significant impact on the Group's future financial results**

- **City Interactive's *Dogfight 1942* receives Xbox 360® certification from Microsoft**

On August 2, 2012 the Management Board of City Interactive S.A. announced that the Company had received confirmation from Microsoft® on the successful completion of the Xbox 360® certification process for *Dogfight 1942*. The Xbox 360® version of the game is set for release on September 4, 2012.

A description of other events which may have a significant impact on the Issuer's future financial results is presented in points XVI and XIX of this report.

**XVIII. Significant risks and threats faced by the Group**

The most significant external risks from the Issuer's point of view are as follows:

**Risk connected with the macroeconomic situation**

The video gaming market in which the City Interactive Group operates is highly competitive, while technology and consumer interests change rapidly. A significant factor which exerts a negative impact on operational efficiency are the macroeconomic fluctuations in specific markets. In order to minimize risk, the Group develops its operations on a global scale, independently releasing products in all of the most significant markets around the world. In recent years the entertainment industry has developed dynamically and it is estimated that the value of the video gaming market will exceed that of the film industry.

**Competition risk**

The City Interactive Group operates in a market where the leading position is held by companies with strong, established positions. The City Interactive Group has proved that it can successfully compete by using its greatest advantages: an experienced team, a global distribution network and cost advantage, connected with a lower profitability threshold in relation to other significantly larger manufacturers. A flat organizational structure is an additional advantage – this brings flexibility and the ability to act quickly. The Group's products are included in all price ranges. Games created for Xbox360®, NINTENDO Wii™, Nintendo DS™, Sony PlayStation®3 and PC have high commercial potential and are competitive in relation to others present in the market. The City Interactive Group has taken significant steps to supplement its product portfolio with games from new segments – online games and games for smartphones.

**Risk of change in trends**

The City Interactive Group operates in the fields of new technology and virtual entertainment, where a product's life cycle is relatively short. What cannot be counted out is the risk of new solutions appearing, meaning that the products offered by the Group cease to be attractive and do not ensure the desired inflows. In order to minimize this risk, a strategy has been adopted to follow trends and offer a product range which is proven and enjoys recognition amongst consumers. A trend-setting strategy would be a lot more expensive and risky.

The City Interactive Group's principal activities in this field are based on constant market monitoring with regard to the development of new technologies (e.g. 3D) and managing new segments created by new consoles.

The number of projects implemented means diversification of the product range and limitation of market risk.

**Risk of change in legal and tax regulations**

Frequent changes in legal and tax regulations in Poland and other markets constitute a threat to the City Interactive Group's operations. This concerns the regulations and interpretation of regulations connected with intellectual property, the capital market, labor law

and social security, tax law and regulations concerning commercial law. In some countries the issue of banning video games containing elements of violence is frequently raised. There is thus a risk of changes in regulations applicable in a country where the Group sells its products, which could turn out to be disadvantageous from the viewpoint of the Group's operations.

The City Interactive Group takes actions aimed at eliminating this risk through cooperation with specialist law firms around the world and through product liability insurance covering the entire product portfolio.

### Foreign exchange risk

During H1 2012, 95% of the Group's revenue was generated in three currencies: EUR, USD and GBP. The Parent hedges against currency risk through incurring liabilities in these currencies. The currency with the highest level of exposure is EUR, followed by USD and GBP.

Cash surpluses in specific currencies are hedged through forward FX contracts in the principal foreign currencies. The following table presents all open forward contracts as at the end of the reporting period.

	Open contracts in foreign currency	Forward initial recognition in PLN	Initial price	Contract settlement date
EUR	300 000	1 315 500	4.3850	March 29, 2013
EUR	1 000 000	4 385 000	4.3850	March 29, 2013
EUR	2 245 000	9 771 812	4.3527	March 29, 2013
USD	450 000	1 444 995	3.2111	March 29, 2013
USD	1 350 000	4 334 175	3.2105	March 29, 2013
USD	2 500 000	8 015 000	3.2060	March 29, 2013
EUR	2 428 964	9 721 929	4.0025	March 29, 2013
		<b>38 988 410</b>		

During the reporting period the Company implemented a hedging policy, according to which the effect of measuring the principal amount, constituting the effective hedge, was recognized in a revaluation reserve (in an amount adjusted for deferred tax). The non-effective part of the contracts (PLN 0.7 million in interest) was recognized in the period's profit and loss. Liabilities resulting from measurement of hedging transactions were presented in the balance sheet under "financial liabilities".

Risks directly connected with the City Interactive Group's operations are as follows:

### Risk of losing key employees

The success of the Group's business is to a large extent dependent on the knowledge and experience of its employees. This is a characteristic feature of gaming manufacturers in a business where the key elements are intellectual assets.

In this market it is difficult to seek out qualified industry specialists. The recruitment of new employees is furthermore combined with the period of their introduction to work, resulting in a temporary period of decreased work efficiency.

The Group places particular emphasis on:

- a motivational salary system which builds links between the organization and the employee, together with medical care and a social package,
- a working environment which encourages communication and sharing of experience,
- management training for key employees,
- an incentive scheme for executives which is conditional on the financial results achieved.



### **Risk associated with the loss of key customers**

This is a risk associated with the termination of distribution agreements or the bankruptcy of entities engaged in distribution. In order to minimize the possibility of incurring losses, the Group's sales operations are conducted on the basis of close cooperation with the largest and most reputable distributors headquartered around the world. Given the specific nature of the US market, the Parent has a US-based subsidiary tasked with continually expanding its distribution capabilities and closely collaborating with the largest distributors.

During H1 2012:

- the largest customer accounted for 17% of the City Interactive Group's total sales,
- the five largest customers accounted for 54% of the Group's sales.

### **Supplier risk**

One of the risk categories connected with suppliers is the release of titles on specific consoles and cooperation with their owners during the certification process. Non-acquisition of certification and the potential for termination of release agreements for consoles are two main elements of risk which exist in reality and may have an impact on the Group's financial results. It should however be emphasized that the Group makes specific efforts to meticulously fulfill and perform all obligations under agreements entered into between such entities and the Issuer or its subsidiaries. Payments connected with the release of games for consoles formed the main part of the Group's commercial liabilities during the reporting period and are always paid on time.

### **Risk connected with the implementation of development plans**

The Parent, City Interactive S.A., has an excess of cash from operating activities, which is used to finance the Group's game releases. The Parent, City Interactive S.A., has the capability to seek bank and financial sector financing in the event of this becoming necessary to finance additional projects.

### **Risk connected with the existing product portfolio**

The video gaming market is driven by expectations connected with the release of new products. There is a risk that some products are finished later than planned, which as a consequence has a negative impact on cash flows generated and the financial result in specific periods.

Internal factors which can cause the delay of a release include difficulties in specifying the time needed to finish production and inspect the quality of a game in order for it to fulfill all expectations relating to quality. The release of a game which does not fulfill the high standards adopted by the Group could have a negative impact not just on the anticipated revenues from sale of this specific product but could also weaken the Company's image.

An external factor capable of resulting in the decision to postpone a release is the market situation, since an important element of the decision-making process is release of a game when competition from other products is at its lowest. Amongst other external factors a significant element is supplier delays in timely preparation of ordered game components.

In many instances rescheduling of a release is connected with an element of marketing known as the "long-awaited game", which is beneficial in creating a product image.

The majority of the Group's products are finished on time and as planned, although the risk of delays cannot be ruled out.

An additional aspect is the risk of companies or external persons threatening Group companies with legal action concerning copyrights to games, their elements, trademarks or reserved names for specific products. Operations in the United States are particularly exposed to this risk since this jurisdiction is characterized by strict legislation. In order to avoid losses here, the Group hires law firms specializing in intellectual property law and registers the trademarks of its products. In submitting such an application to protect trademarks in the European Union and in other countries around the world, availability in specific markets is verified and the risk of violating third party trademarks is estimated.

### **Liquidity risk**

The City Interactive Group currently has a financial surplus and receivables fully cover its payables, which eliminates liquidity risk. Protection against the risk of purchaser insolvency is ensured through analyzing their financial condition and constantly monitoring payment of receivables. It should additionally be emphasized that the Parent is able to raise capital through bank debt or the issue of bonds on highly favorable terms.

### **XIX. Indication of factors which the Issuer's management considers as potentially having an effect on the Company's financial results over at least the next half-year**

The City Interactive Group is unwavering in pursuing its development strategy aimed at consistently releasing high quality video games. Currently, the quality of the game development, marketing and sales process is the decisive factor impacting product planning and development activities. The Group is systematically increasing development of games for next-generation consoles. This is a clear move in the direction of the most important global market, where sales are based on console products, while at the same time following the latest gaming trends. The management is expanding operations by venturing into new genres and gaming models (role-playing games – RPG, free-to-play – F2P) and new distribution channels (games for iOS systems, i.e. the iPad®, iPhone® and iPod Touch®, as well as online and social games), which constitutes a further step in the Group's development. The Issuer's management believes that this will yield a further improvement in City Interactive S.A.'s financial performance in subsequent quarters and years.

The City Interactive Group plans to release a new game in September 2012 – *Dogfight 1942*, which will be chiefly distributed online for Xbox360®, Sony PlayStation®3 and PC. The game presents spectacular dogfights from the major air battles of the Second World War. A sophisticated damage system, scale of military operations and the extensive range of aircraft available in the game make *Dogfight 1942* one of the leading titles in this market segment. This is to be a completely new brand which, as was the case with *Sniper: Ghost Warrior*, will fill a niche in the market.

December 2012 will see the release of *Alien Fear*, a science fiction-styled first-person shooter in which players assume the role of the sole surviving member of a marines unit on a mission to rescue the crew of a missing spacecraft – Deep Space One. The game is being developed based on the latest version of Unreal® Engine3 and will be available chiefly in online distribution for Xbox360®, Sony PlayStation®3 and PC.

For almost two years intensive work has been underway on the production of *Sniper: Ghost Warrior 2*, a sequel to *Sniper: Ghost Warrior*. The improved second game in the series is based on the latest CryENGINE®3 technology and has a good chance of becoming the Issuer's all-time largest production and distribution success. It will be able to compete with the largest global titles in the FPS segment. The realism of the gameplay and story, coupled with a shooting mechanism which is improved on the previous version, make the game something completely new and a pioneering experience in tactical sniper simulation aimed at a broad consumer base. The release of *Sniper: Ghost Warrior 2*, scheduled for January 15, 2012, will undoubtedly be one of the most important factors impacting the Group's financial results in 2013. Additional content will be introduced following the game's release, including add-ons, which will further drive sales revenue for *Sniper: Ghost Warrior 2*.

The Group is also working on an iOS version of *Sniper: Ghost Warrior* for the iPad® and iPhone®, which will be developed using Epic Games Inc.'s Unreal® Engine3. This release is planned for Q4 2012 / Q1 2013.

Another one of the Issuer's key projects in the production phase with high commercial potential is *Enemy Front*, a first person shooter set during the Second World War. Production of the game is being handled by two of the Issuer's studios in Rzeszow, Poland, and

Guildford in the UK. *Enemy Front* is a classic of the genre, developed around a highly popular topic, however with a modern approach using one of the most up-to-date and advanced technologies for FPS development – CryENGINE®3. Some of the team at the Issuer's Romanian studio will also be working on development of the game – they will support the work of the Rzeszow studio, in particular developing multi-player functionality (online gaming), which is intended as a significant element of *Enemy Front*.

The game is set behind Nazi lines over several years in various historically significant locations. The game's release for Xbox360®, Sony PlayStation®3 and PC is planned for the first half of 2013. City Interactive S.A.'s management is counting on an equally impressive reception for the game as was the case with *Sniper: Ghost Warrior*.

Work is currently underway on the development of *Lords of the Fallen*, primarily in Germany where an experienced team at Deck13 Interactive GmbH is working alongside the game's executive producer Tomasz Gop (one of the principal producers of *The Witcher® 2 Assassins of Kings*). Its release on Xbox360®, Sony Playstation®3 and PC is planned for H2 2013.

From August 2011 the Company's Romanian development studio has been working on City Interactive's first free-to-play project – *World of Mercenaries*. The game is set to be a modern online multiplayer shooter. It is scheduled for release in 2013.

The Issuer's management believes that the current strategy will allow City Interactive S.A. to achieve further financial success, strengthen its position in global markets and diversify Group revenues. The management believes that the company has the necessary competences and technical capabilities to develop and release high quality games.

#### Release plan for 2012-2013:

Game	Platform	Date
Dogfight 1942	PS®3 / XBOX360® / PC	September 4, 2012
Alien Fear	PS®3 / XBOX360® / PC	December 2012
Sniper: Ghost Warrior 2	PS®3 / XBOX360® / PC	January 15, 2013
Sniper: Ghost Warrior	Android™/iOS	Q1 2013
Enemy Front	PS®3 / XBOX360® / PC	H1 2013
World of Mercenaries	Online	2013
Lords of the Fallen	PS®3 / XBOX360® / PC	H2 2013

#### XX. Information on agreements with an entity authorized to audit financial statements

- a) Name of the entity: CSWP Audyt Spółka z ograniczoną odpowiedzialnością Sp. k.
- b) Date of entering into the agreement on audit of the separate and consolidated financial statements for 2012 – May 28, 2012. The agreement concerns audit of the financial statements of the Parent and Group for 2012 (semi-annual review and annual audit).
- c) Total remuneration due for review and audit of the Parent's and Group's financial statements in 2012 – PLN 40 000 net.



**Marek Tymiński**

President of the Management Board

**Andreas Jaeger**

Member of the Management Board

Warsaw, August 30, 2012

