



Unofficial translation from Estonian

Avaron Emerging Europe Small Cap Fund

Annual Report for the Financial Year 2008

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Fund Facts

Avaron Emerging Europe Small Cap Fund (hereinafter: „the Fund”) is registered in the Republic of Estonia as a contractual open-ended investment fund the units of which are publicly offered. The Fund complies with the requirements set out in the Council Directive 85/611/EEC of 20 December 1985.

Name of the Fund	Avaron Emerging Europe Small Cap Fund
Fund management company	AS Avaron Asset Management
Registered address and contact details of the fund management company	Address: Narva road 5-58, Tallinn 10117, Estonia Phone: +372 66 44 200 Facsimile: +372 66 44 201 E-mail: info@avaron.ee www.avaron.ee
Depository	AS Swedbank
Auditor	AS Deloitte Audit Eesti
Supervisor	Estonian Financial Supervision Authority
Fund managers	Valdur Jaht, Peter Priisalm
Fund established	3 April 2007
Start of the Fund's activities	23 April 2007
Financial year	01 January 2008 – 31 December 2008

Management Report

Avaron Emerging Europe Small Cap Fund (hereinafter: „the Fund”) started its activities on 23 April 2007. The value of the assets of the Fund totalled EEK 102 million as at the end of the 2008 financial year (31.12.2007: EEK 388 million). Avaron Emerging Europe Small Cap Fund invests in listed small and medium sized companies in Emerging Europe countries. As at the end of the financial year, Poland and Austria were the major countries among the Fund’s investments portfolio. Due to the market circumstances, a substantial share of the Fund’s assets was also held in cash and deposits.

2008 will be a year long remembered. The share prices dropped sharply at the Central and Eastern European and other emerging markets as well as the developed markets. The net asset value of the Fund’s A and B unit declined by 64.2% and 64.0% during the financial year, respectively (during the period from 23.04.2007 to 31.12.2007: -11.7% and -11.2%, respectively).

We believe that the coming 6-12 months will continue to be difficult for the equity markets as the economic crisis that got a start from the USA property market in 2007 is starting to have an even more substantial effect on the real economy. Basically, the whole world has witnessed a severe decline in industrial production and rapidly rising unemployment. Further possible increases in unemployment have eroded consumer confidence, who are postponing non-critical purchases as much as possible. For many companies, this has translated into reduced demand both at the home market as well as abroad.

The effects of the credit crisis started seriously hitting Eastern Europe in the final quarter of 2008. However, tighter credit and the higher cost of risk shall be mostly reflected in the real economy of the Eastern European countries only in 2009. It is estimated that it will bring about forced liquidations and push down asset prices. However, the number of transactions should start increasing and liquidity should improve. This implies that the more adaptable companies should find new opportunities.

Resulting from the above arguments, we have positioned the Fund much more defensively than previously. We have increased the share of non-cyclical companies with a strong balance sheet that could improve their market share during the difficult times owing to their strong cash position or that have high dividend yields. We have also substantially increased the liquidity of the Fund by reducing the share of small cap companies and keeping a larger portion of the Fund’s assets in cash and deposits. However, a certain portion of the Fund’s investment portfolio is still made up of cyclical companies as we see potential in this segment following the drastic drop in prices that took place in 2008. Additionally, we are prepared to increase the share of cyclical companies further, once we spot the first signs for sustainable economic growth.

Valdur Jaht
Fund Manager and
Member of the Management Board of the fund management company

Confirmation of the Management Board of the Fund Management Company to the Financial Statements for 2008

The Management Board of the fund management company has prepared the Financial Statements of Avaron Emerging Europe Small Cap Fund on March 23, 2009.

The Financial Statements have been prepared in compliance with the requirements stipulated in the Estonian Accounting Act, the Investment Funds Act and Accounting Principles Generally Accepted in Estonia and it gives a true and fair view of the assets, liabilities, net asset value and performance results of Avaron Emerging Europe Small Cap Fund. The Management Board considers Avaron Emerging Europe Small Cap Fund to carry its activities as a going concern.

The Financial Statements of Avaron Emerging Europe Small Cap Fund have been approved by the fund management company and the fund managers.

Name	Position	Signature	Date
Kristel Kivinurm-Priisalm	Chairman of the Management Board of the fund management company		23 March 2009
Valdur Jaht	Member of the Management Board of the fund management company/ Fund manager		23 March 2009
Peter Priisalm	Fund manager		23 March 2009

Balance Sheet

In Estonian kroon

	Note	31.12.2008	31.12.2007
ASSETS			
Securities			
Shares and fund units		63,810,760	316,504,335
Bonds		3,112,409	0
Derivative instruments	3	3,373,025	954,960
Total securities		70,296,194	317,459,295
Deposits			
Cash and bank accounts		14,442,438	45,714,012
Term deposits		16,427,775	0
Structured deposits		0	20,040,211
Total deposits		30,870,213	65,754,223
Other assets			
Accrued income		127,555	4,591
Miscellaneous receivables		682,519	5,003,699
Total other assets		810,074	5,008,290
TOTAL ASSETS		101,976,481	388,221,808
LIABILITIES AND NET ASSET VALUE			
Liabilities			
Payables to the management company		124,446	473,062
Payables to the depository		25,008	68,837
Payables for redeemed fund units		91,158	2,041,879
Total liabilities		240,612	2,583,778
Net asset value of the fund	4	101,735,869	385,638,030
TOTAL LIABILITIES AND NET ASSET VALUE		101,976,481	388,221,808

Statement of Income and Expenses

In Estonian kroon

INCOME	01.01-31.12.2008	23.04-31.12.2007
Net gain from investments		
From shares and units		
Sales profit/(-loss)	-158,918,385	-9,329,669
Unrealised profit /(-loss)	-61,285,522	-38,138,931
Dividends	5,691,910	1,533,722
Total from shares and units	-214,511,997	-45,934,878
From bonds		
Unrealised profit /(-loss)	14,599	0
Interest income	11,009	0
Total from bonds	25,608	0
From deposits		
Interest income	859,415	1,275,987
The change in fair value of structured deposits	-251,782	251,782
Total from deposits	607,633	1,527,769
From derivative instruments		
Sales profit/(-loss)	9,322,697	-375,445
Unrealised profit /(-loss)	2,846,921	-352,547
Total from derivative instruments	12,169,618	-727,992
Total net gain from investments	-201,709,138	-45,135,101
Other income		
Net gain/(loss) from transactions in foreign currencies	-11,865,162	-771,411
Other financial income	0	1,856
Total other income	-11,865,162	-769,555
TOTAL INCOME	-213,574,300	-45,904,656
EXPENSES		
Operating expenses		
Management fee	3,585,485	3,422,995
Performance fee	0	3,620,484
Depository fee	513,092	490,430
Transaction costs	296,252	161,705
Total operating expenses	4,394,829	7,695,614
Other expenses		
Other expenses	4,610	0
Total other expenses	4,610	0
TOTAL EXPENSES	4,399,439	7,695,614
NET RESULT OF THE FUND	-217,973,739	-53,600,270

Statement of Investments

In Estonian kroon as of 31.12.2008

Name	Issuer	Country	Nominal value	FX	Quantity	Avg acq cost per unit	Avg acq cost	Mrkt value per unit	Total mrkt value	Share of market value of fund's assets, %
Shares and units										
A AND D PHARMA HOLDINGS NV DR	A & D PHARMA HOLDINGS NV	RO	1	EUR	9,668	192.04	1,856,649	34,26	331,261	0.32%
AB SA	AB SA	PL	1	PLN	98,395	75.80	7,458,288	13,29	1,307,458	1.28%
ADVANCE TERRAFUND SHARE	ADVANCE TERRAFUND REIT JSC	BG	1	BGN	448,553	16.13	7,236,499	8,88	3,982,718	3.91%
ARCO VARA SHARE	ARCO VARA AS	EE	10	EEK	337,189	12.57	4,238,139	2,66	896,896	0.88%
AS EESTI TELEKOM LIHTAKTSIA	EESTI TELEKOM AS	EE	10	EEK	16,100	63.23	1,018,070	61,02	982,422	0.96%
BULGARIA REAL ESTATE FUND	BULGARIA REAL ESTATE FUND	BG	1	BGN	566,083	9.44	5,346,303	6,79	3,844,418	3.77%
CITY SERVICE AB	CITY SERVICE AB	LT	1	LTL	184,045	49.16	9,047,349	15,35	2,825,700	2.77%
ELANA AGRICULTURAL LAND OPPORT	ELANA AGRICULTURAL LAND OPPORT	BG	0	BGN	200,000	18.53		7,14	1,428,645	1.40%
EQUEST BALKAN PROPERTIES PLC	EQUEST BALKAN PROPERTIES PLC	GB	0.01	GBP	340,000	26.34	8,954,783	4,78	1,626,537	1.60%
ERSTE GROUP BANK AG	ERSTE GROUP BANK AG	AT	0	EUR	15,644	565.90	8,852,995	253,46	3,965,083	3.89%
FARMACOL SHARE	FARMACOL S.A.	PL	1	PLN	55,263	168.66	9,320,860	107,44	5,937,556	5.82%
FLAMINGO	FLAMINGO	RO	0.1	RON	1,289,700	1.83	2,362,475	0,11	144,150	0.14%
HRVATSKI TELEKOM DD	HRVATSKI TELEKOM DD	HR	100	HRK	5,000	553.24	2,766,181	422,92	2,114,584	2.07%
IMMO EAST IMMOBILIEN ANLAGEN	IMMO EAST IMMOBILIEN ANLAGEN	AT	1	EUR	482,064	35.68	17,198,052	7,20	3,469,381	3.40%
INDYKPOL SA COMMON STOCK	INDYKPOL SA	PL	5	PLN	13,614	431.67	5,876,813	88,00	1,198,080	1.17%
INTER CARS SA	INTER CARS SA	PL	2	PLN	1,254	249.21	312,514	101,56	127,353	0.12%
LC ROMANIA PROPERTY FUND LTD	LEWIS CHARLES ROMANIA	GB	1.4	GBP	243,572	32.56	7,929,738	1,47	358,533	0.35%
MECANICA CEHLAU PIATRA NEAMT	MECANICA CEHLAU PIATRA NEAMT	RO	0.1	RON	1,455,000	1.75	2,540,517	0,46	664,644	0.65%
MONDI PACK PAPER SWIECIE SA	MONDI PACK PAPER SWIECIE SA	PL	1	PLN	9,553	393.51	3,759,188	150,72	1,439,850	1.41%
PANEVEZIO STATYBOS TRESTAS	PANEVEZIO STATYBOS TRESTAS	LT	1	LTL	55,948	75.69	4,234,752	6,79	380,083	0.37%
PEGAS NONWOVENS CZK	PEGAS NONWOVENS SA	LU	1	CZK	24,200	305.07	7,382,813	135,85	3,287,509	3.22%
POLSKI KONCERN NAFTORNY ORLEN	POLSKI KONCERN NAFTOWAY ORLEN	PL	1.25	PLN	25,600	153.86	3,938,873	97,68	2,500,729	2.45%
RAIFFEISEN BANK	RAIFFEISEN BANK	AT	1	EUR	15,944	836.34	13,334,666	301,96	4,814,421	4.72%
SIF BANAT CRISANA(RO)	SIF BANAT CRISANA	RO	0	RON	166,300	17.75	2,952,120	2,13	353,968	0.35%
SIF MOLDOVA (RO)	SIF MOLDOVA	RO	0	RON	223,200	10.34	2,307,039	2,07	462,064	0.45%
SIF MUNTENIA(RO)	SIF MUNTENIA	RO	0	RON	471,700	10.04	4,736,151	2,42	1,141,546	1.12%
SIF OLTENIA (RO)	SIF OLTENIA	RO	0	RON	168,500	12.01	2,023,398	2,28	384,854	0.38%
SPARKASSEN IMMOBILIEN AG	SPARKASSEN IMMOBILIEN AG	AT	0	EUR	46,629	151.10	7,045,455	30,98	1,444,477	1.42%
TELEFONICA O2 C.R. SHARE	TELEFONICA O2 C.R.	CZ	100	CZK	25,700	241.79	6,213,993	247,90	6,370,949	6.25%
TEO LT AB	TEO LT AB	LT	1	LTL	501,275	6.18	3,096,841	5,25	2,633,518	2.58%
VIENNA INSURANCE GROUP	VIENNA INSURANCE GROUP	AT	1	EUR	4,750	714.46	3,393,703	377,37	1,792,505	1.76%
ZEMAITIJOS PIENAS	ZEMAITIJOS PIENAS	LT	1	LTL	624,830	8.81	5,504,455	2,56	1,598,868	1.57%
Total shares and units							175,946,640		63,810,760	62.57%

Member of the Management Board:

Statement of Investments (cont.)

In Estonian kroon as of 31.12.2008

Name	Issuer	Country	Maturity	Nom. value	FX	Quantity	Avg acq cost per unit	Avg acq cost	Mrkt value per unit	Total mrkt value	Interest rate	Share of market value of fund's assets, %
Bonds*												
TALLINNA SADAM FRN 17.03.09	TALLINNA SADAM AS	EE	2009-03-16	1,000	EUR	200,000	1,548.90	3,097,809	1,556.20	3,162,668	7.95	3.10%
Total bonds								3,097,809		3,162,668		3.10%
<i>*Accrued interest in the amount of EEK 50,259 has been added to the value of bonds; the accrued interest is recorded in the balance sheet under "Accrued income"</i>												
Derivative instruments												
FX OPT EUR/PLN @ 3.5524 08APR9	HANSAPANK	EE	2009-04-08	1	EUR			356,248		2,611,781		2.56%
FX OPTION EUR/RON@4.0 02FEB09	HANSAPANK	EE	2009-02-02	1	EUR			164,278		230,882		0.23%
FX OPTION EUR/RON@4.1 05JAN09	HANSAPANK	EE	2009-01-05	1	EUR			114,994		17,900		0.02%
FXOPTION EUR/CZK@26.12 21APR09	HANSAPANK	EE	2009-04-21	1	EUR			243,131		512,462		0.50%
Total derivative instruments								878,651		3,373,025		3.31%
Total securities								179,923,100		70,346,453		68.98%
Deposits*												
Current account										12,829,751		12.58%
DEPOSIT-HANSAPANK(EUR)	HANSAPANK	EE	2009-01-12		EUR			1,955,688		1,965,303	5.90	1.93%
DEPOSIT-HANSAPANK(EUR)	HANSAPANK	EE	2009-01-07		EUR			782,275		782,400	5.75	0.77%
DEPOSIT-HANSAPANK(EUR)	HANSAPANK	EE	2009-01-12		EUR			1,955,688		1,965,303	5.90	1.93%
DEPOSIT-HANSAPANK(EUR)	HANSAPANK	EE	2009-01-12		EUR			1,955,688		1,965,303	5.90	1.93%
DEPOSIT-HANSAPANK(EUR)	HANSAPANK	EE	2009-01-12		EUR			1,955,688		1,965,303	5.90	1.93%
DEPOSIT-HANSAPANK(EUR)	HANSAPANK	EE	2009-01-12		EUR			1,955,688		1,965,303	5.90	1.93%
DEPOSIT-HANSAPANK(EUR)	HANSAPANK	EE	2009-01-12		EUR			1,955,688		1,965,303	5.90	1.93%
DEPOSIT-HANSAPANK(EUR)	HANSAPANK	EE	2009-01-12		EUR			1,955,688		1,965,303	5.90	1.93%
DEPOSIT-HANSAPANK(EUR)	HANSAPANK	EE	2009-01-12		EUR			1,955,688		1,965,303	5.90	1.93%
O/N DEPOSIT -HANSAPANK(EEK)	HANSAPANK	EE	2009-01-01		EEK			1,612,687		1,612,934	5.50	1.58%
Total deposits								18,040,466		30,947,509		30.35%
<i>*Accrued interest in the amount of EEK 77,296 has been added to the value of deposits; the accrued interest is recorded in the balance sheet under „Accrued income“</i>												
Total investments								197,963,566		101,293,962		99.33%
Other assets												
Miscellaneous receivables (unsettled transactions)										682,519		0.67%
Total other assets										682,519		0.67%
TOTAL ASSETS										101,976,481		100.00%

Statement of Investments

In Estonian kroon as of 31.12.2007

Name	Issuer	Country	Nominal value	Currency	Quantity	Avg acq cost per unit	Avg acq cost	Mrkt value per unit	Total mrkt value	Share of market value of fund's assets, %
Shares and units										
A AND D PHARMA HOLDINGS NV DR	A & D PHARMA HOLDINGS NV	GB	1	EUR	9,668	192.04	1,856,649	242.51	2,344,541	0.60%
AB PIENO ZVAIGZDES	AB PIENO ZVAIGZDES	LT	1	LTL	154,000	21.57	3,321,246	26.25	4,041,815	1.04%
AB SA	AB SA	PL	1	PLN	63,600	102.05	6,490,063	115.83	7,366,681	1.90%
ACTION SA	ACTION SA	PL	0.1	PLN	40,000	95.49	3,819,409	143.81	5,752,373	1.48%
ADVANCE TERRAFUND SHARE	ADVANCE TERRAFUND REIT JSC	BG	1	BGN	218,553	16.36	3,575,157	16.24	3,548,915	0.91%
AS EESTI TELEKOM LIHTAKTSIA	EESTI TELEKOM AS	EE	10	EEK	153,000	126.95	19,422,903	122.04	18,672,120	4.81%
AUTOMOTIVE COMPONENTS EUROPE	AUTOMOTIVE COMPONENTS EUROPE	PL	0.15	PLN	241,592	81.54	19,699,121	51.19	12,367,106	3.19%
BETACOM SA	BETACOM SA	PL	1	PLN	95,850	90.35	8,659,863	72.01	6,902,457	1.78%
BULGARIA REAL ESTATE FUND	BULGARIA REAL ESTATE FUND	BG	1	BGN	291,083	12.14	3,533,480	17.04	4,959,515	1.28%
CITY SERVICE AB	CITY SERVICE AB	LT	1	LTL	43,045	58.65	2,524,613	60.24	2,592,846	0.67%
DEBICA	DEBICA	PL	8	PLN	5,929	392.54	2,327,380	456.37	2,705,831	0.69%
EQUEST BALKAN PROPERTIES PLC	EQUEST BALKAN PROPERTIES PLC	IE	0.01	GBP	340,000	26.34	8,954,783	17.23	5,859,881	1.51%
ERSTE BANK	ERSTE BANK	AT	1	EUR	23,000	743.9	17,109,769	758.81	17,452,555	4.49%
FABIAN ROMANIA PROPERTY FUND	FABIAN ROMANIA PROPERTY FD LTD	GB	0	EUR	450,000	20.59	9,266,384	19.48	8,765,391	2.26%
FARMACOL SHARE	FARMACOL S.A.	PL	1	PLN	80,518	173.89	14,001,616	183.07	14,740,389	3.80%
FIRMA HANDLOWA JAGO S.A	FIRMA HANDLOWA JAGO S.A	PL	1	PLN	179,973	14.31	2,575,940	13.93	2,506,201	0.65%
FIRST INVESTMENT BANK	FIRST INVESTMENT BANK	BG	10	BGN	93,284	86.84	8,101,070	92.79	8,655,815	2.23%
FLAMINGO	FLAMINGO	RO	0	RON	1,289,700	1.83	2,362,475	1.5	1,935,446	0.50%
GRAJEWO SA	GRAJEWO SA	PL	3	PLN	30,000	195.78	5,873,289	229.92	6,897,642	1.78%
GRUPA KETY SA	GRUPA KETY SA	PL	3	PLN	9,000	657.1	5,913,884	694.1	6,246,921	1.61%
GRUPA KOLASTYNA SHARE	GRUPA KOLASTYNA SA	PL	1	PLN	577,517	19.35	11,175,029	12.36	7,140,245	1.83%
IMMO EAST IMMOBILIEN ANLAGEN	IMMO EAST IMMOBILIEN ANLAGEN	AT	1	EUR	271,390	130.62	35,447,836	115.31	31,293,258	8.06%
IMMOEAST IMMOBILIEN ANLG - WSE	IMMO EAST IMMOBILIEN ANLAGEN	AT	1	PLN	19,790	126.43	2,502,058	113.62	2,248,458	0.58%
INDYKPOL SA COMMON STOCK	INDYKPOL SA	PL	5	PLN	9,814	440.68	4,324,847	496.72	4,874,780	1.26%
LC ROMANIA PROPERTY FUND LTD	LEWIS CHARLES ROMANIA	GB	1	GBP	293,572	32.56	9,557,540	28.25	8,292,282	2.14%
LC SOFIA PROPERTY FUND	LEWIS CHARLES BULGARIA	GB	1	GBP	389,000	22.9	8,909,733	17.77	6,911,319	1.78%

Statement of Investments (continued)

In Estonian kroon as of 31.12.2007

Name	Issuer	Country	Nominal value	Currency	Quantity	Avg acq cost per unit	Avg acq cost	Mrkt value per unit	Total mrkt value	Share of market value of fund's assets, %
Shares and fund units (cont.)										
LENA LIGHTNING S.A.	LENA LIGHTNING S.A.	PL	0.05	PLN	229,833	44.24	10,168,891	22.12	5,084,943	1.31%
MECANICA CEHLAU PIATRA NEAMT	MECANICA CEHLAU PIATRA NEAMT	RO	0.1	RON	1,212,500	2.1	2,540,517	2.7	3,269,991	0.84%
MEINL INTERNATIONAL POWER	MEINL INTERNATIONAL POWER LTD	AT	10	EUR	80,000	152.76	12,220,700	83.08	6,646,208	1.71%
MONDI PACK PAPER SWIECIE SA	MONDI PACK PAPER SWIECIE SA	PL	1	PLN	13,003	393.45	5,116,064	294.56	3,830,159	0.99%
PANEVEZIO STATYBOS TRESTAS	PANEVEZIO STATYBOS TRESTAS	LT	1	LTL	79,438	75.38	5,987,671	70.43	5,594,497	1.44%
PEGAS NONWOVENS CZK	PEGAS NONWOVENS SA	LU	1	CZK	20,000	437.84	8,756,732	436.19	8,723,709	2.25%
POLSKY KONCERN MIESNY DUDA	POLSKY KONCERN MIESNY DUDA SA	PL	1	PLN	351,513	38.81	13,642,318	32.54	11,436,843	2.95%
PROSPER SA	PROSPER SA	PL	1	PLN	44,055	84	3,700,660	71.58	3,153,426	0.81%
RICHTER GEDEON (DEMAT)	GEDEON RICHTER	HU	1,000	HUF	3,100	2,231.13	6,916,517	2,564.84	7,950,992	2.05%
ROKISHKIO SHURIS	ROKISHKIO SHURIS	LT	1	LTL	50,000	35.55	1,777,536	35.8	1,790,087	0.46%
SIF BANAT CRISANA(RO)	SIF BANAT CRISANA	RO	0.1	RON	256,300	16.94	4,340,485	15.44	3,957,766	1.02%
SIF MOLDOVA (RO)	SIF MOLDOVA	RO	0.1	RON	275,000	16.39	4,507,722	15.14	4,162,796	1.07%
SIF MUNTENIA(RO)	SIF MUNTENIA	RO	0.1	RON	407,800	11.65	4,751,759	10.48	4,275,013	1.10%
SIF OLTENIA (RO)	SIF OLTENIA	RO	0.1	RON	260,000	19.45	5,058,188	18.88	4,908,358	1.26%
SPARKASSEN IMMOBILIEN AG	SPARKASSEN IMMOBILIEN AG	AT	0	EUR	75,000	153.83	11,537,594	120.94	9,070,479	2.34%
TEO LT AB	TEO LT AB	LT	1	LTL	1,670,082	10.63	17,749,569	10.76	17,964,028	4.62%
UNIMA 2000 SA	UNIMA 2000 SYSTEMY SA	PL	1	PLN	123,829	68.63	8,497,819	31.89	3,948,328	1.02%
ZEMAITIJOS PIENAS	ZEMAITIJOS PIENAS	LT	10	LTL	55,000	86.27	4,744,637	102.94	5,661,929	1.45%
Total shares and fund units							353,321,516		316,504,335	81.52%
Derivative instruments										
					Due date					
ERSTEBANK FEB08 PUT@ 46	HANSAPANK	EE	1	EUR	2008-02-16					
ERSTEBANK FEB08 PUT@ 48	HANSAPANK	EE	1	EUR	2008-02-16					
EUR/PLN 3.66 CALL 07MAR2008	HANSAPANK	EE	1	EUR	2008-03-07					
EUR/RON 3.607 CALL 07MAR2008	HANSAPANK	EE	1	EUR	2008-03-07					
EUR/RON 3.633 CALL 05MAR2008	HANSAPANK	EE	1	EUR	2008-03-05					

Statement of Investments (continued)

In Estonian kroon as of 31.12.2007

Name	Issuer	Country	Nominal value	Currency	Due date	Avg acq cost per unit	Avg acq cost	Mrkt value per unit	Total mrkt value	Share of market value of fund's assets, %
Derivative instruments (cont.)										
FX OPTION EUR/PLN@3.67 05MAR08	HANSAPANK	EE	1	EUR	2008-03-05		264,722		155,722	0.04%
Total derivative instruments							1,307,507		954,960	0.25%
Total securities							354,629,023		317,459,295	81.77%
Deposits*										
				Interest (%)	Due date					
CURRENT ACCOUNT		EE							2,804,708	0.72%
OVERNIGHT DEPOSIT-HANSAPANK(EEK)	HANSAPANK	EE	5.2500	EEK	2008-01-01		1,775,725		1,775,985	0.46%
OVERNIGHT DEPOSIT-HANSAPANK(EUR)	HANSAPANK	EE	3.7910	EUR	2008-01-01		41,133,579		41,137,910	10.60%
HP DEPOSIT RICHTER 08.01.08	HANSAPANK	EE		EUR	2008-01-08		19,788,428		20,040,211	5.16%
Total Deposits							62,697,732		65,758,814	16.94%
<i>*Accrued interest in the amount of 4,590.57 has been added to the value of deposits; the accrued interest is recorded in the balance sheet under „Accrued income”.</i>										
Total investments							417,326,755		383,218,109	98.71%
Other assets										
Miscellaneous receivables (unsettled transactions)									5,003,699	1.29%
Total other assets									5,003,699	1.29%
TOTAL ASSETS									388,221,808	100%

Distribution of Investments

	31.12.2008		31.12.2007	
	Amount	Share	Amount	Share
Securities listed on stock exchanges	66,923,168	65.6%	315,549,375	81.3%
Other securities	3,373,025	3.3%	954,960	0.2%
Cash, deposits, miscellaneous receivables and accrued income	31,680,288	31.1%	71,717,473	18.5%
Total	101,976,481	100.0%	388,221,808	100.0%

Statement of Changes in Net Assets

In Estonian kroon

	01.01-31.12.2008	23.04-31.12.2007
Net asset value at the beginning of the period	385,638,030	0
Cash received for fund units issued	11,174,162	476,264,310
Cash paid for fund units redeemed	-76,936,469	-36,859,325
Subscription and redemption fees (total) paid to the fund management company	-166,115	-66,685
Net result of the Fund	-217,973,739	-53,600,270
Net asset value at the end of the period	101,735,869	385,638,030
Number of A units in circulation at the end of the period:	679,576.209	1,062,734.488
Number of B units in circulation at the end of the period:	2,511,150.502	3,284,521.779
Net asset value of an A unit at the end of the period:	31.6084	88.3119
Net asset value of an B unit at the end of the period:	31.9597	88.8367

Notes to the Financial Statements

Note 1. Accounting Policies and Assessments Used

The financial statements of Avaron Emerging Europe Small Cap Fund (hereinafter „the Fund“) for 2008 have been prepared in compliance with the effective Investment Funds Act as supplemented by the regulations of the Minister of Finance, and the Accounting Principles Generally Accepted in Estonia. The requirements of the Accounting Principles Generally Accepted in Estonia comply with the internationally acknowledged accounting and reporting principles and are stipulated in the Estonian Accounting Act, which is supplemented by the guidelines issued by the Estonian Accounting Standards Board.

The balance sheet and the statement of income and expenses and the notes to the financial statements have been prepared in accordance with the Minister of Finance Regulation No. 50 of 02.07.1998 "Requirements for the Annual and Semi-Annual Reports of Investment Funds". The financial statements have been prepared in Estonian kroon, unless a reference to another currency is made. The main accounting principles used when preparing the financial statements have been set out below.

Report period

The fund started its activities on April 23, 2007. Consequently, the comparative data for the previous financial year has been presented for the period April 23, 2007 - December 31, 2007.

Foreign currency transactions

Upon recording foreign currency transactions, the last bid rate established by the depository for the funds managed by AS Avaron Asset Management on the transaction date has been used (hereinafter referred to as the depository bid rate). The assets and liabilities fixed in foreign currency are translated into Estonian kroon based on the depository bid rate applicable on the balance sheet date.

Gains and losses from foreign currency transactions are recorded in the statement of income and expenses under "Gain/ (loss) from transactions in foreign currencies" on net basis.

Financial assets and liabilities

Financial assets include securities, deposits, accrued income, other receivables and derivative instruments with positive market value. Financial liabilities include accrual-based liabilities to the management company and depository and other liabilities as well as derivative instruments of negative market value. Financial assets and liabilities are initially recorded at cost, which is the fair value of the consideration paid or received to acquire the financial asset or liability. The initial acquisition cost includes all the expenses directly related to the financial asset or liability. The financial assets and liabilities are recorded in the balance sheet at the moment when the right of ownership is transferred to the Fund in accordance with the terms and conditions of the financial asset or liability contract.

Securities

Shares, units of investment funds, bonds, derivative instruments, structured bonds and other securities are recorded as securities in the balance sheet. The transaction date method is used when accounting for securities. Securities are initially recognised at acquisition cost, which is the fair value of the consideration paid for the security. The acquisition cost includes all direct expenses related to acquiring the financial asset. Securities are later accounted for in accordance with the following principles:

- The market value of shares traded on a regulated market is determined on the basis of the official closing price on the balance sheet date. If the closing price is unavailable, the official mid price is used. If mid price is also unavailable, the last official bid price is used.
- The value of bonds not traded on a regulated market is determined based on the average of the bid and ask quotes as provided by the price feed service provider being used. If the quotes are not available or if the quotes do not reflect the fair value of the bond in the opinion of the fund management company, the price is determined based on the yield curve method.
- The value of options not traded on a regulated market is determined based on the Black & Scholes valuation model. The inputs that are necessary for the calculation are determined by the fund management company after consulting with the counterparty of the option.

Unrealised gains/ (losses) from revaluation of securities are recorded in the statement of income and expenses under "Unrealised profit/ (loss)" on the corresponding instrument.

Securities are removed from the balance sheet when the fund has lost control over the corresponding financial assets either as a result of selling them or expiry of their term. When accounting for realised gains/ (losses) from securities transactions, the FIFO method is used. The line „Sales profit/ (loss)“ in the statement of income and expenses indicates the difference between the sales amount of an instrument and the corresponding acquisition cost. The sales amount of securities is the quantity of securities sold multiplied by the sales price less paid commissions.

Deposits

Cash and deposits are valued at nominal value. The balances of current accounts, overnight deposits and time deposits are recorded under deposits. Accrued interest on deposits is recorded as accrued income.

In order to determine the value of structured bonds and structured deposits, the bond or deposit is divided into separate components (for example deposit plus option). The value of each component is determined in accordance with the principles set out in the procedure for calculating net asset value. In order to determine the total value of the instrument, the values of different components are summed up.

Other assets

Other assets include other revenues calculated on the accrual basis but not received yet, incl. interest, other similar receivables, dividend receivables, and other accrued income. Miscellaneous receivables include receivables from unsettled sale transactions.

Liabilities

Liabilities include management fee and performance fee payables to the fund management company, and depository fee and transaction fee payables to the depository. Liabilities also include payables to fund unit-holders for redeemed units. Miscellaneous liabilities include payables for securities purchase transactions the value date of which is after the balance sheet date.

Recognition of income and expenses

Sales revenue and expenditure is recorded on the accrual basis when all the essential risks relating to ownership have passed to the buyer and the sales revenue (expenditure) and the expenses relating to a transaction can be reliably established. Received dividends are recognised under “Dividends” at the moment when the shareholder’s right to the dividend is fixed.

The operating expenses of the fund include the management fee and performance fee payable to the management company, the depository fee payable to the Fund’s depository and transaction fees. Transaction fees related to security purchase and sales transactions are recorded under “Transaction fees” in the statement of income and expenses. Commissions which arose and were paid in acquisition of securities, but are not clearly identifiable are included within the acquisition cost of securities.

Note 2. Statement of Commissions

In Estonian kroon

01.01.2008 - 31.12.2008

	Number of transactions	Volume of transactions	Total commissions paid	Weighted average fee
Securities traded on Tallinn Stock Exchange				
Swedbank (AS Hansapank)	10	7,960,655	-	0.00%
SEB	12	15,451,371	-	0.00%
Evli Securities	2	8,115,006	-	0.00%
Other securities traded in Estonia				
Swedbank (AS Hansapank)	36	38,698,443	-	0.00%
Securities traded on stock exchanges of other countries or OTC				
Swedbank (AS Hansapank)	4	8,058,803	-	0.00%
BRE Securities	13	8,090,236	-	0.00%
Concorde Securities	3	10,258,314	-	0.00%
UniCredit CAIB	22	33,382,610	-	0.00%
Erste Bank	186	357,223,942	-	0.00%
First Financial Brokerage House	11	7,668,267	-	0.00%
Bank Handlowy	65	56,305,211	-	0.00%
ING Bank	2	4,215,335	-	0.00%
Ipopema Securities	70	90,447,262	-	0.00%
Lewis Charles Securities	2	2,025,468	-	0.00%
Patria Finance	64	137,068,685	-	0.00%
KBC Securities	18	20,557,509	-	0.00%
Other Avaron funds and clients	2	3,601,025	-	0.00%
SEB	22	18,380,337	-	0.00%
Evli Securities	2	3,907,154	-	0.00%
Banco Espirito Santo de Investimento	40	21,410,304	-	0.0%
Total	586	852,825,937	-	0.00%

23.04.2007. – 31.12.2007

	Number of transactions	Volume of transactions	Total commissions paid	Weighted average fee
Securities traded on Tallinn Stock Exchange				
AS Hansapank	3	5,654,228	161,705	0.00%
AS SEB Pank	1	3,249,005	-	0.00%
AS Suprema Securities	5	16,497,390	-	0.00%
Other securities traded in Estonia				
AS Hansapank	14	60,722,592	-	0.00%
Securities traded on stock exchanges of other countries or OTC				
BRE Securities	2	4,304,801	-	0.00%
Concorde Securities	18	47,461,341	-	0.00%
Unicredit CAIB	6	4,550,509	-	0.00%
Erste Bank	34	99,732,747	-	0.00%
First Financial Brokerage House	5	19,452,861	-	0.00%
AS Hansapank	1	2,524,613	-	0.00%
Bank Handlowy	21	25,512,594	-	0.00%
H. Rivkin & Co	1	8,807,019	-	0.00%
ING Bank	1	303,652	-	0.00%
Ipopema Securities	163	179,547,718	-	0.00%
AS Lõhmus, Haavel & Viisemann	2	1,671,875	-	0.00%
Lewis Charles Securities	7	37,262,501	-	0.00%
Meinl Bank	2	12,220,700	-	0.00%
Patria Finance	5	11,565,054	-	0.00%
AS SEB Pank	4	10,893,163	-	0.00%
AS Suprema Securities	31	36,696,820	-	0.00%
Swiss Capital	33	52,959,344	-	0.00%
Avaron Balkan Fund	4	9,808,445	-	0.00%
Karoll	2	3,575,157	-	0.00%
KBC Securities	2	5,424,908	-	0.00%
Total	367	660,399,037	161,705	

Note 3. Statement of Derivative Instruments

31.12.2008

Type of instrument	Issuer of the instrument	Name and quantity of underlying	Exercise date	Premium/ price of instrument	Exercise price		Market value		Equity of the issuer of the instrument
					per unit	total	per unit	total	
Put option	AS Hansapank	19,328,800 CZK	21/04/2009	15,540 EUR	26.120	740,000 EUR	0.69	512,462 EEK	29.5 bn EEK
Put option	AS Hansapank	5,328,600 PLN	08/04/2009	22,770 EUR	3.552	1,100,000 EUR	2.37	2,611,781 EEK	29.5 bn EEK
Put option	AS Hansapank	1 600 000 RON	02/02/2009	10,500 EUR	4.000	400,000 EUR	0.58	230,882 EEK	29.5 bn EEK
Put option	AS Hansapank	1,230,000 PLN	05/01/2009	7,350 EUR	2.100	300,000 EUR	0.06	17,900 EEK	29.5 bn EEK
Total	X	X	X	X	X	2,540,000 EUR	X	3,373,025 EEK	X

31.12.2007

Type of instrument	Issuer of the instrument	Name and quantity of underlying	Exercise date	Premium/ price of instrument	Exercise price		Market value		Equity of the issuer of the instrument
					per unit	total	per unit	total	
Put option	AS Hansapank	ERSTE BANK 7,500	2/15/2008	EUR 14,475	46.00	EUR 345,000	18.7918	EEK 140,939	EEK 22,073,300,000
Put option	AS Hansapank	ERSTE BANK 5,000	2/15/2008	EUR 10,716	48.00	EUR 240,000	31.3965	EEK 156,982	EEK 22,073,300,000
Put option	AS Hansapank	RON PUT 2,179,800	3/5/2008	EUR 12,420	3.633	EUR 600,000	0.2376	EEK 142,589	EEK 22,073,300,000
Put option	AS Hansapank	PLN PUT 8,808,000	3/5/2008	EUR 16,920	3.670	EUR 2,400,000	0.0649	EEK 155,722	EEK 22,073,300,000
Put option	AS Hansapank	RON PUT 2,164,200	3/7/2008	EUR 12,600	3.607	EUR 600,000	0.2843	EEK 170,580	EEK 22,073,300,000
Put option	AS Hansapank	PLN PUT 8,784,000	3/7/2008	EUR 16,440	3.660	EUR 2,400,000	0.0784	EEK 188,149	EEK 22,073,300,000
Total	X	X	X	X	X	6 585 000 EUR	X	954 960 EEK	X

Note 4. Comparative Analysis of the Net Asset Value

In Estonian kroon

	31.12.2008	31.12.2007
Net asset value of the Fund	101,735,869	385,638,030
Net asset value of A unit	31.6084	88.3119
Net asset value of B unit	31.9597	88.8367

Note 5. Other Information

The fund's portfolio turnover ratio amounted to 163% in 2008. The portfolio turnover ratio is computed by taking the lesser of purchases or sales and dividing by average monthly net assets.

The total expense ratio (including management, performance and depository fees) equalled 1.99% of net asset value for A units and 1.48% for B units.

[TRANSLATION FROM ESTONIAN]

INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Avaron Emerging Europe Small Cap Fund and Fund Manager:

We have audited the accompanying annual accounts (page 5 to 18) of Avaron Emerging Europe Small Cap Fund, which comprise the balance sheet as at 31 December 2008, the profit and loss statement for the year then ended, statement of investments and net assets value statement, and a summary of significant accounting policies and other explanatory notes.

Fund Manager's Management Board Responsibility for the Annual Accounts

Management Board of Fund Manager AS Avaron Asset Management is responsible for the preparation and fair presentation of these annual accounts in accordance with Law of Investment Funds, Estonian Accounting Act and the guidelines issued by Estonian Accounting Standards Board. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of annual accounts that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility


Our responsibility is to express an opinion on these annual accounts based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the annual accounts are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the annual accounts. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the annual accounts, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Fund's preparation and fair presentation of the annual accounts in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Management Board of Fund Manager, as well as evaluating the overall presentation of the annual accounts.

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

Opinion

In our opinion, the annual accounts present fairly, in all material respects, the financial position of Avaron Emerging Europe Small Cap Fund as of 31 December 2008, and its financial performance for the year then ended in accordance with Law of Investment Funds, Estonian Accounting Act and the guidelines issued by Estonian Accounting Standards Board.


Veiko Hintsov
Certified Auditor
13 April 2009


AS Deloitte Audit Eesti