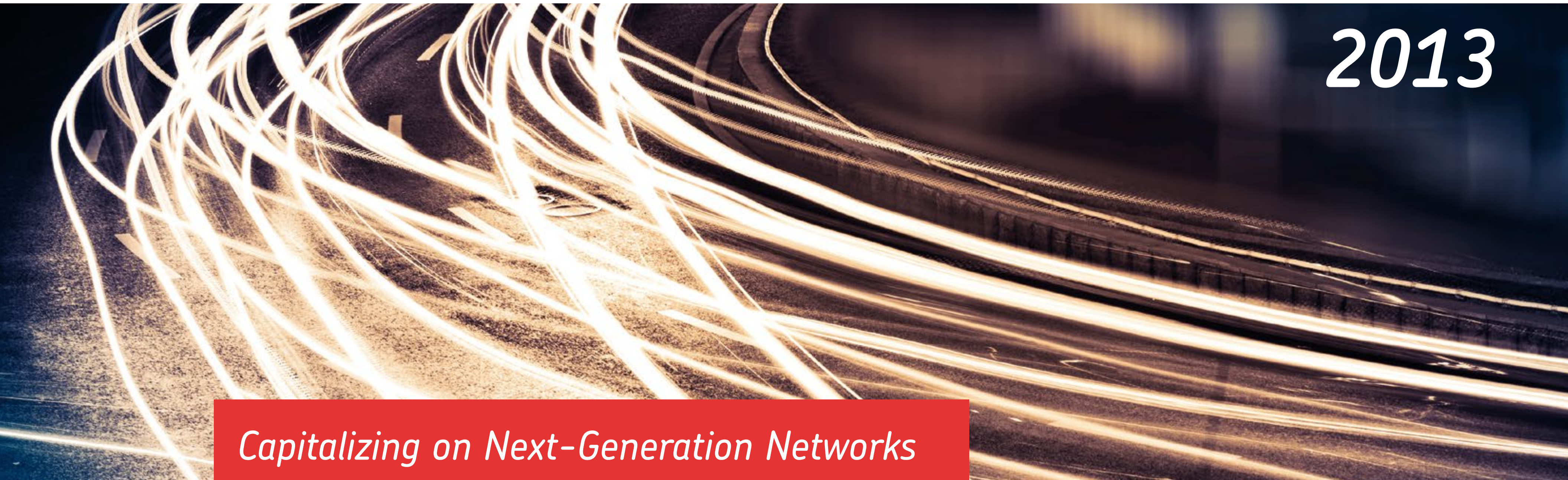
Annual Report 2013



Capitalizing on Next-Generation Networks

ADVA™ Optical Networking

Welcome

Profile

At ADVA Optical Networking we're creating new opportunities for tomorrow's networks, a new vision for a connected world.

Our intelligent telecommunications hardware, software and services have been deployed by several hundred service providers and thousands of enterprises.

Over the past twenty years, our innovative connectivity solutions have helped to drive our customers' networks forward, helped to drive their businesses to new levels of success.

We forge close working relationships with all our customers. As their trusted partner we ensure that we're always ready to exceed their networking expectations.

Mission

ADVA Optical Networking enables next-generation networks. The Company's mission is to be the trusted partner for innovative connectivity solutions that *ADVANCE* next-generation networks for cloud and mobile services.

ADVAntages

Focus on Growth Markets

- ADVA Optical Networking focuses on growth markets in the telecom space that have one thing in common: a strong and sustainable demand for Optical+Ethernet connectivity.
- These markets are driven by the shift from legacy purpose-built networks to next-generation multi-purpose networks, where Optical+Ethernet technology provides the underlying foundation.
- Average growth across these markets is expected to be 12% per year between 2013 and 2016 to a total of USD 13.4 billion in 2016.[1]

Optical+Ethernet Innovation

- ADVA Optical Networking's industry-leading engineering force is exclusively focused on Optical+Ethernet innovation, outperforming the engineering departments of other vendors in this space.
- Focus on innovation drives market success and has made ADVA Optical Networking one of the two leading players worldwide for fiber-based Ethernet access devices with a market share of 18%[2] and …
- … a strong competitor in Europe, Middle East and Africa (EMEA) in the metro and long-haul optical market with a market share of 7%.[3]

Speed for Customers

- ADVA Optical Networking has a strong track record of being first to market with new functionality that adds value for customers.
- A responsive team serves customers around the globe, with 66% of ADVA Optical Networking's 2013 revenues generated in EMEA, 28% in the Americas and 6% in Asia-Pacific.
- ADVA Optical Networking's Optical+Ethernet solutions have been deployed by several hundred service providers and thousands of enterprises around the globe.

Trusted Partner

- ADVA Optical Networking's unique combination of innovation and speed has seen the Company build close partnerships with customers, resulting in repeat purchases and strong cross-selling opportunities for its Optical+Ethernet solutions.
- As a trusted partner for two decades, ADVA Optical Networking provides high-quality solutions with lowest cost of ownership and best user experience.
- The Company's experienced management team has many years of senior management background in blue-chip telecommunications equipment companies, making it a dependable partner when it comes to building long-term business relationships.

[1] Industry analyst estimates for metro and long-haul WDM equipment ("Optical") and Ethernet access devices ("Ethernet") relevant to ADVA Optical Networking. Sources: Infonetics Research Optical Network Hardware, Quarterly Market Share, Size, and Forecasts 3Q13, November 2013, and Infonetics Research Ethernet Access Devices Biannual Market Share, Size and Forecasts, 2nd Edition, September 2013.

[2] Based on 2012 total revenues for Ethernet access devices relevant for ADVA Optical Networking. Source: Infonetics Research Ethernet Access Devices Biannual Market Share, Size and Forecasts, 2nd Edition, September 2013.

[3] Based on 2012 total revenues for optical transport equipment relevant for ADVA Optical Networking. Source: Infonetics Research Optical Network Hardware, Quarterly Market Share, Size, and Forecasts 3Q13, November 2013.

Contents

ADVAntages at work

Innovation

Driving new ideas in an industry that is continually evolving. Turn to *pages 20, 24 and 28* to read more about ADVA Optical Networking's innovative network solutions.

Speed for Customers

Ensuring your data is where you need it, when you need it. Read more about ADVA Optical Networking's commitment to its customers' needs on *pages 32 and 50.*

Trusted Partner

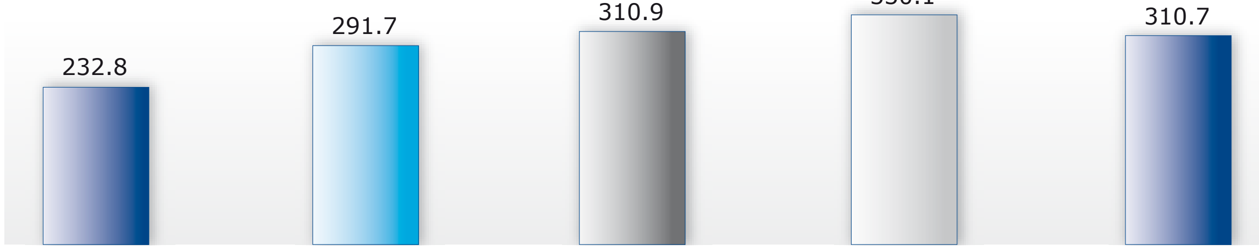
Fostering relationships that help building the network of the future. Turn to *pages 86 and 166* to discover how ADVA Optical Networking is working with its customers and partners to enable sustainable growth.

2013 Financial Highlights

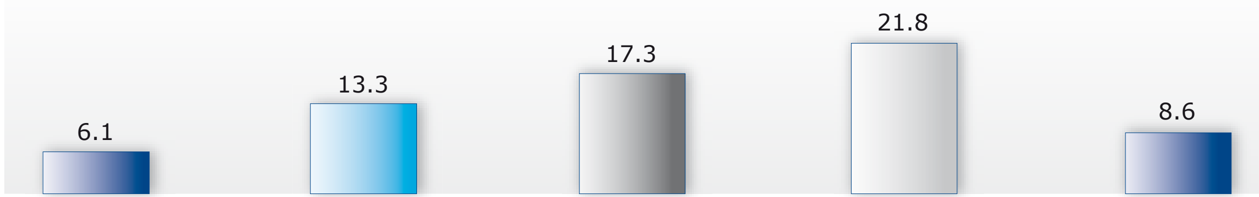
(in millions of EUR)

● 2009 ● 2010 ● 2011 ● 2012 ● 2013

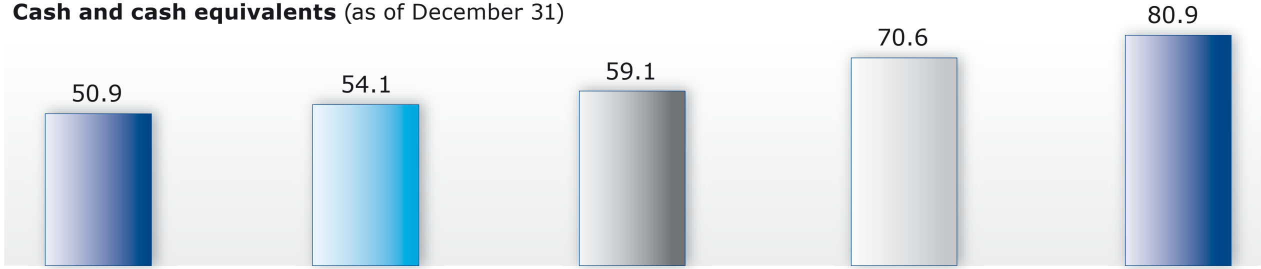
Revenues



Pro forma operating income (IFRS)*



Cash and cash equivalents (as of December 31)



* Pro forma operating income is calculated prior to non-cash charges related to the stock compensation programs and amortization and impairment of goodwill and acquisition-related intangible assets.

2013 Business Highlights

- Volatile revenue development, but sustained profitability and financial strength

- Ongoing innovation leadership and further international expansion, sound technology and distribution partnerships

- Strong focus on above-average margin enterprise networks business

During 2013, ADVA Optical Networking made the following key announcements:

Customer Achievements

- January 22: The Croatian government's national electricity company, Hrvatska Elektroprivreda (HEP), has deployed the country's first 100G technology, using ADVA Optical Networking's FSP 3000. The two companies – in collaboration with their regional partner ITeRATIO – conducted a successful 100G deployment over a distance of more than 400km between the Croatian cities of Zagreb and Split. This success highlights the government's commitment to developing the country's network infrastructure and will significantly boost HEP's network capacity and performance.

- April 9: Kabel Deutschland, the largest cable operator in Germany, has selected ADVA Optical Networking's 100G coherent transport for a new nationwide backbone network. Forming part of ADVA Optical Networking's Agile Core solution, Kabel Deutschland deploys 100G technology along with multi-degree, directionless ROADMs. Consisting of 26 major nodes and more than 50 intermediate sites, this network includes a fully meshed backbone throughout Germany.

- May 7: Hetzner Online has deployed ADVA Optical Networking's 100G Core technology throughout its backbone network. One of Germany's leading web-hosting providers and data center operators, Hetzner Online is using ADVA Optical Networking's 100G coherent solution to respond to fierce growth in video traffic and other bandwidth-intensive applications. Hetzner Online was able to rapidly deploy the ADVA 100G Core by plugging it into its existing 10G network.

- May 29: Zen Internet, a leading provider of award-winning Internet services to business and home users in the United Kingdom, has chosen ADVA Optical Networking's FSP 150 to scale its Ethernet delivery platform and efficiently hand over services to service provider partners. Integrated Etherjack™ technology provides Zen with comprehensive levels of service intelligence and end-to-end monitoring while a partnership with Imtech ICT UK ensures an always-on network.

- June 20: The Cactus Group, the leading retailer in Luxembourg, has deployed ADVA Optical Networking's FSP 3000 to provide optical data center connectivity in order to rollout a new, fully redundant data center infrastructure. The ADVA FSP 3000 will be the foundation for the Cactus Group's business continuity applications, ensuring that its operations are always online and running. The solution was deployed by ADVA Optical Networking's long-standing partner, Telindus.

- August 6: U.S.-based Northwest Open Access Network (NoaNet) has selected ADVA Optical Networking's 100G Core technology to cope with the enormous bandwidth growth in Washington State, partly supported by the Broadband Technology Opportunities Program, which services unserved and underserved communities in this region. NoaNet's network reaches some of the most rural regions of Washington State, providing high-speed broadband and Internet services. The new 100G Core project builds on fruitful cooperation between ADVA Optical Networking and NoaNet established in 2005.

- September 5: Openreach, the infrastructure division of BT Group in the United Kingdom has installed over 100,000 of ADVA Optical Networking's FSP 150 circuits for its Ethernet Access Direct services. This number represents an important milestone in one of the world's largest Ethernet based transmission networks. One of the key reasons for this success is the FSP Management Suite that enables Openreach to drastically simplify the provisioning of new services and rapidly respond to customer requests.

- September 25: Brazilian carrier OptiTel is using ADVA Optical Networking's FSP 3000 as the foundation for an ambitious network expansion. Initially focusing upon cities within southern Brazil, OptiTel is deploying the FSP 3000 to capitalize on continued bandwidth demand from its customers. A key competitive advantage for OptiTel is its 4000km of fiber connecting the provinces of Rio Grande Do Sul, Santa Catarina, Paraná and São Paulo. One of the principal reasons for the selection of the FSP 3000 was its proven single-fiber working capabilities.

- October 1: JSC Fortex, a voice and Internet service provider in the Moscow area in the Russian Federation, has deployed ADVA Optical Networking's 100G Metro throughout Moscow and the surrounding regions. With a network covering over 3,000km of fiber, JSC Fortex is using the ADVA 100G Metro primarily to upgrade existing 10G services and prepare for increased bandwidth demand from its mix of business and residential customers. The ADVA 100G Metro was specifically selected by JSC Fortex because of its plug-and-play simplicity, especially when upgrading existing services.

- October 9: Bangkok's Stock Exchange of Thailand has deployed ADVA Optical Networking's FSP 3000 for mission-critical storage area network connectivity. Focusing primarily upon business continuity and disaster recovery applications, the ADVA FSP 3000 was specifically chosen because of its proven success in other financial networks around the world. The Thailand Stock Exchange is now able to transport information between data centers with low latency, high availability and robust security.

- October 29: DB Systel, one of the leading providers of ICT services in Germany, has selected the ADVA Optical Networking's FSP 3000 to support metro and long distance network applications for its holding company Deutsche Bahn, Germany's major railway provider. The frame agreement with system integrator Axians is based upon ADVA Optical Networking technology for connectivity solutions of multiple 10Gbit/s. This connectivity enables DB Systel to flexibly meet bandwidth requirements in its network.

- November 19: SysEleven has deployed ADVA Optical Networking's FSP 3000 to answer fierce bandwidth demand. As one of the leading Internet service providers in Berlin, Germany, SysEleven has expanded its network several times in the preceding twelve months to accommodate continued customer growth. The ADVA FSP 3000 connects SysEleven's data centers within the city, ensuring robust, reliable and secure optical transport for its customers' cloud-based and virtualized applications. The network was deployed is maintained by ADVA Optical Networking's Elite partner Axians.

- December 4: inexio, a service provider in southwestern Germany, has deployed ADVA Optical Networking's 100G Metro for regional connectivity in Germany and Luxembourg. Operating one of Europe's fastest growing networks, inexio is harnessing the ADVA 100G Metro to respond to significant bandwidth growth from both its enterprise and residential customers. A long-standing customer of ADVA Optical Networking and its Elite partner Axians, inexio has benefited from the native scalability of the ADVA FSP 3000, gradually expanding its network infrastructure with customer demand. With over 5,000km of fiber, inexio will be making further 100G deployments in 2014.

New Products and Solutions – Innovation

- February 19: ADVA Optical Networking demonstrated its new Cachejack™ technology during Mobile World Congress 2013. Cachejack™ is designed to improve mobile user experience and enable location-based services (LBS) through an application-aware radio access network and optimize resource utilization by uniquely transporting content directly from the backhaul network straight to the mobile subscriber. Cachejack™ accelerates downloading of content such as video streaming and high-resolution images from the Internet. The new capability was added through ADVA Optical Networking's Q4 2012 investment in Saguna Networks. Improving user experience, enabling new revenue-generating LBS and reducing transport costs are of prime value to today's mobile operators.

- June 18: ADVA Optical Networking announced that its FSP 150 family of mobile backhaul products now includes an IEEE 1588v2 mini-grandmaster (miniGM) clock and boundary clock functionality. The integration of the miniGM ensures precise frequency and time synchronization at the network edge and is specifically designed to support the large-scale rollout of small cells for LTE-Advanced and radio access networks operating in unpaired spectrum. The development of the miniGM is the latest in a series of updates to the ADVA FSP 150 Syncjack™ timing distribution and assurance technology that is designed to simplify the migration to LTE and LTE-Advanced radio access networks.

- July 17: ADVA Optical Networking announced that its FSP 150 is capable of delivering sub-microsecond timing accuracy for time-critical high performance trading applications. This improves the synchronization of financial transactions from thousandths of a second to millionths of a second. Thus the FSP 150 brings a competitive advantage to the members of the finance and investment community.

- September 16: ADVA Optical Networking introduced an industry-first Software-Defined Networking (SDN) solution in cooperation with IBM and Marist College. They have successfully demonstrated a virtualized optical transmission network using OpenFlow-based control. Before, the virtualization of the physical network that interconnects data centers had not been possible. SDN and related software makes the network more dynamic and responsive, thus not only meeting the fierce bandwidth demand, but also improving the end user experience.

Interoperability and Alliance Partnerships

- March 27: ADVA Optical Networking launched its Partner Ecosphere Program (PEP). The new program provides the Company's partners with a comprehensive suite of tools designed to help expand their business and increase profitability. These services include ready access to state-of-the-art lab facilities, on-demand web-based trainings and a global support base. PEP currently offers two partnership levels: Elite and Select. Each level is targeted at specific business demands as well as service and quality requirements.

- April 17: ADVA Optical Networking announced the Company's presentation at the 2013 Telcordia NIST-ATIS Workshop on Synchronization in Telecommunication Systems, on April 18, in San Jose, California, USA. Sponsored by NIST, Telcordia and ATIS-COAST, WSTS'13 provided a forum for high-level discussion and knowledge sharing among synchronization experts.

- June 6: Colt Technology Services used ADVA Optical Networking's FSP 3000 to support Germany's largest film festival in Berlin, enabling over 400 screenings to more than 300,000 ticket buyers and 20,000 professionals from the international film community. ADVA Optical Networking provided the FSP 3000 to power a 10Gbit/s backbone link supporting high-definition video distribution to over 40 screens connected to a fiber-optic network provided by Colt Technology Services.

- June 26: ADVA Optical Networking announced that its 16Gbit/s Fibre Channel (FC) card is the first in the networking industry to achieve Brocade qualification. Following completion of interoperability testing as part of Brocade's Gen 5 FC program, the ADVA 16Gbit/s FC card will be a key component for enterprises seeking to evolve their high-density server virtualization, cloud architectures and storage applications.

- September 19: ADVA Optical Networking announced the demonstration of its synchronization delivery and assurance technology at ISPCS 13 Plugfest. Designed specifically for the industry, ISPCS 13 Plugfest enables vendors to test the interoperability of new technologies in a live environment and resolve any compatibility issues that may arise. ADVA Optical Networking attended the event for the first time showcasing a number of devices, including its FSP 150SP sync probe.

- November 5: ADVA Optical Networking announced the hosting of multiple seminars at ITSF 2013, held in Lisbon, Portugal, on the importance of timing and synchronization assurance in mobile backhaul networks. ADVA Optical Networking hosted two key seminars during this time that further explained to the industry why performance-based synchronization is critical in high-performance LTE and LTE-Advanced networks. These seminars showcased vital strategies that mobile network operators will need to adopt if they are to meet the challenges ahead.

- November 18: ADVA Optical Networking, Juniper Networks and the University of Michigan announced that they are showcasing a demo at SC13 that clearly defines the future of big data transport. Comprised of a globally dispersed OpenFlow network, the demo revealed how research and education organizations can efficiently scale their networks to effectively transport multiple petabytes of data – something that is critical to collaborative scientific research. The demo was built around Juniper Networks' PTX Series Packet Transport Routers, including their integrated 100G coherent transponder and ADVA Optical Networking's 100G Core technology.

Company Events

- March 31: The number of members of ADVA Optical Networking’s Management Board has been reduced from four to three. At the end of Q1 2013, Christian Unterberger, Chief Sales & Marketing Officer, left the Company by mutual agreement. Christian was instrumental in driving revenues through a comprehensive and proactive global program, determining product positioning and market launch strategies, as well as promoting ADVA Optical Networking’s global brand identity. His areas of responsibility have been assumed by Chief Executive Officer Brian Protiva. Besides Brian, ADVA Optical Networking’s Management Board still consists of Christoph Glingener (Chief Technology Officer) and Jaswir Singh (Chief Financial Officer & Chief Operating Officer).

- June 24: ADVA Optical Networking announced that it has won the prestigious Supply Chain Management Award. This annual award is presented to the company with the most effective value chain in the manufacturing industry. The awarding bodies believed that ADVA Optical Networking’s global end-to-end and cross-enterprise segmentation is unique within the manufacturing industry and provides the Company with a clear competitive edge. The award was presented by the management consulting unit of PricewaterhouseCoopers and the trade journal Logistik Heute, in partnership with the Institute for Supply Chain Management and the House of Logistics and Mobility.

- July 5: ADVA Optical Networking announced that its 100G Metro has won an acclaimed eco Internet award. The 100G Metro enables service providers and enterprises to answer bandwidth demand in the metro environment while also driving down costs. Claiming first place in the “Carrier Category”, ADVA Optical Networking’s 100G Metro was recognized as a real innovation in the networking industry.

Management Board

From left to right:

Jaswir Singh, Brian Protiva and Christoph Glingener

Members and Their Backgrounds

ADVA Optical Networking is led by a dynamic, international, experienced and highly-motivated team. Leading, directing and managing the Company's growth are three executive officers:

Brian Protiva
Chief Executive Officer

Christoph Glingener
Chief Technology Officer

Jaswir Singh
Chief Financial Officer & Chief Operating Officer

Brian Protiva
Chief Executive Officer (CEO)

Bachelor of Science in Electrical Engineering, Stanford University, USA

Brian Protiva co-founded ADVA Optical Networking in 1994. As the CEO, he is responsible for overall strategy, human resources, quality management, sales and marketing. Under Brian's leadership, ADVA Optical Networking advanced to become a global market leader in Ethernet access devices and one of the top players in metro Wavelength Division Multiplexing (WDM) worldwide. To date, ADVA Optical Networking's innovative Optical+Ethernet solutions have been deployed in more than 10,000 enterprises and more than 250 carrier networks around the world. Revenues reached EUR 311 million in 2013, while employment climbed to 1,425 employees at year-end 2013. Prior to ADVA Optical Networking, Brian was managing director at AMS Technologies (now the EGORA Group), which he joined in 1987 and where he focused on co-managing its subsidiaries.

Christoph Glingener
Chief Technology Officer (CTO)

Ph.D. in Electrical Engineering, University of Dortmund, Germany

Christoph Glingener joined ADVA Optical Networking in April 2006, assuming responsibility for all global research and development activities at sites in Europe, the United States and China. In 2007, Christoph was appointed CTO. Since that time, he also leads ADVA Optical Networking's product management and advanced technology teams. Christoph has focused on streamlining ADVA Optical Networking's product portfolio, defining the product strategy and building the Company's standing as a global innovator in optical networking. Christoph's activities at ADVA Optical Networking build on a long and successful industry career with experience gained in both academic and corporate roles. These include leading positions at Marconi Communications (now Ericsson) and Siemens Communications (now Coriant).

Jaswir Singh
Chief Financial Officer (CFO) & Chief Operating Officer (COO)

Master of Advanced Business Practice, University of South Australia, Australia
Master of Accountancy, with Distinction, Charles Sturt University, Australia
Bachelor of Commerce, University of Canterbury, New Zealand
Member of CPA Australia

Jaswir Singh joined ADVA Optical Networking in November 2007 to enable the Company's next growth stage. Since joining the Company, he has worked to solidify ADVA Optical Networking's financial position, including strengthening the balance sheet, improving internal controls and processes to ensure accuracy of financial statements, implementing strategies to manage working capital, improve cash generation, cash flow and net liquidity, and minimizing foreign currency exposure. In early 2009, Jaswir also assumed the COO function, whereby he manages the Company's global manufacturing, supply chain and logistics activities. Additionally, in July 2009, he took over responsibility for the Company's global business systems and information technology activities, and also assumed the role of president of the Company's North American subsidiary, maintaining full legal responsibility for the region. Jaswir has a long and successful background with global telecommunications and high-tech companies, including the North American subsidiary of Nokia; AirDefense (now part of Motorola Solutions); and Equant (a division of the France Telecom Group now known as Orange Business Services). Jaswir has more than 20 years experience in senior general management, CFO and operations roles, including managing USD multi-billion enterprises globally.

Letter to Shareholders

Dear shareholders and friends,

2013: Disappointing revenue development, but ongoing financial strength and profitability as well as strong focus on winning higher-margin business, innovation, international expansion, cost containment and flexibility

The easing of the EUR zone crisis, softer monetary policies and reasonable economic growth resulted in global stock market indices posting record highs in 2013, albeit at uneven growth rates. While developed countries recorded the strongest growth rates, most notably the U.S., emerging market indices in many cases recorded negative returns. Global inconsistencies were also highlighted in a challenging demand environment for telecommunications equipment and solutions. While U.S. service providers increased capital expenditures, especially in H1 2013, growth slowed again in H2 2013, and full-year growth rates slowed down in the Asian-Pacific region and even turned negative in Europe. With temporary shifts in carrier investment priorities, these developments were reflected in ADVA Optical Networking's negative revenue trend, which clearly contrasts with the expectations we had a year ago.

We maintained financial strength and profitability. After light demand from select major customers, our quarterly revenues in 2013 stabilized at levels of between EUR 76 million and EUR 79 million, with revenues up sequentially in Q2 and Q3. In an extremely challenging environment, revenues for Q4 2013, at EUR 76.2 million, came in at the upper end of guidance of between EUR 71 million and EUR 76 million. These results were supported by our expanding customer base. Throughout the year, ADVA Optical Networking maintained financial strength, with an equity ratio north of 50% and high net liquidity levels at all quarterly balance sheet dates. At year-end 2013, our cash and cash equivalents even reached a quarter-end record high of EUR 80.9 million. Even with the disappointing 2013 revenue development, we remained profitable in all quarters of the year.

Strong focus on above-average margin enterprise networks business. We have moved to a model of continuing investments in strategic initiatives and aggressively managing costs while winning new footprint. Although 2013 developed disappointingly and we struggled to build momentum and grow, ADVA Optical Networking's pipeline continues to expand, and there are clear signs that we will return to growth. Creating opportunities to focus our solutions on specific customer needs and drive better margin contribution, we continue to expand into various new verticals like health care, utilities and media. These opportunities will lead to better customer diversification, contributing to less volatile top and bottom line growth. As a technology-driven company, we will address a number of new opportunities for growth, which should also help to expand our margins over time. The transition from hype to implementation of mainstream cloud services and a software-centric network is materializing. "Video, mobility, and cloud services are causing carriers to redesign their networks. About 35% of service providers were re-architecting their networks in 2013, and more will join them in 2014, distributing many functions in the metro. These distributed functions include broadband remote access servers, content delivery networks and caching, deploying servers and storage in 'mini data centers' for colocation and cloud services, and the ability to offer services (such as security) to residential and business customers using network functions virtualization (NFV) with software-defined network (SDN) service chaining."[1]

[1] Source: Infonetics Research's Top 2014 Trends, January 2014.

With the shift to SDN and NFV, ADVA Optical Networking can differentiate its products and bring more value to its market. Infonetics Research projects the data center and enterprise SDN market will top USD 3 billion by 2017,[2] and that coherent 100G technology will arrive in volume in metro networks in 2016.[1] Enterprises are rapidly adopting the use of cloud computing, needing to transform the way they operate and compete in an increasingly competitive market environment. This is providing many new opportunities for our Optical+Ethernet connectivity solutions.

Ongoing innovation leadership and further international expansion. We have continued to invest in further innovation during the last quarters, burdening profitability, but we have been able to secure new and strategic customers for the future. New product cycles and market-leading technology launches will be the catalyst for improved shareholder value. In 2013, we continued to bring new features and capabilities to the market and we continued to differentiate ourselves with technology. New releases for the mobile backhaul segment included adding capabilities to our 10G demarcation solutions as well as caching solutions for the mobile networks. We also developed the mini-grandmaster clock functionality, the latest in a series of updates to the FSP 150 Syncjack™ timing distribution and assurance technology developed to simplify the migration to LTE-Advanced radio access networks, thereby helping carriers upgrade existing service edge routers and switches. For data center connectivity, our ultra-compact 16Gbit/s Fibre Channel card, the first of its kind to achieve Brocade qualification,

[2] Source: Infonetics Research Data Center and Enterprise Hardware and Software Market Size and Forecasts, December 2013.

expands the capabilities of our FSP 3000 platform and is a key component for enterprises seeking to evolve their high-density server virtualization, cloud architectures and storage applications. In September 2013, as an industry-first SDN solution, ADVA Optical Networking successfully demonstrated a virtualized optical transmission network using OpenFlow-based control, developed in partnership with IBM and Marist College. With our innovative connectivity solutions portfolio including state-of-the art Ethernet access synchronization and assurance features as well as our 100G encryption technology for both metro and regional networks, ADVA Optical Networking is well positioned to benefit from these technology trends. Furthermore, our professional partner program increases our access to new market verticals. This program has been embraced by our existing and new potential partners as it enables them with co-op funding, coordinated marketing support, certification and a sophisticated e-learning initiative. Our strategic plan is to increase revenue growth through this partner program and to have a broader sales and support staff whereby our own specialists can then spend more focused time on acquiring new customers and embracing new market verticals. And finally, having a professional partner program will allow us to quickly build support infrastructure for customers in new regions or for global accounts. Our investments in research & development continued to support our ability to win new accounts and expand into new applications with existing customers.

We continued to increase efficiency and achieved higher flexibility. The challenging global economic environment forced many of our customers to curtail investments, which combined with our industry's short delivery cycles resulted in poor visibility and little ability to map the future. Considering this volatility, in 2013 ADVA Optical Networking remained disciplined about its operational costs, enabling us to adapt quickly with a strong focus on sustainable profitability. With strict controls in place and continually maintaining a strong cash position, ADVA Optical Networking's balance sheet is deemed best-in-class by financial analysts. With our market-leading efficiency and delivery performance underlining our brand promise, ADVA Optical Networking won the prestigious annual supply chain management award in 2013, presented annually to the company with the most effective value chain in the manufacturing industry. The awarding bodies believed ADVA Optical Networking's global end-to-end and cross-enterprise segmentation is unique and provides us with a clear competitive edge.

2014: Increasing profitability in the likely case of ongoing market and revenue growth coupled with increasing margins and an ongoing focus on innovation

Looking ahead to 2014 and beyond, despite the continued strengthening of the U.S. and a recovering European economy, industry analysts remain either mixed or conservative in their growth estimates for the telecommunications industry. Infonetics Research points to “2014 as the 4th year of a new investment cycle”, citing AT&T’s USD 14 billion Velocity IP project and Deutsche Telekom’s EUR 30 billion investment plan – both announced in Q4 2012 and scheduled for the next 3 years – and more recently, Vodafone’s GBP 7 billion Project Spring capex plan. Moreover, massive LTE rollouts in Brazil, China and Russia will bring additional fuel to our forecast. This is rebalancing worldwide capex that was mainly localized in Japan and the U.S. through H1 2013. In addition, enterprise cloud service adoption is accelerating. Investment in data centers and their requisite technologies will remain robust in the near term, and enterprises are investing to improve application performance, increase security, and reduce costs. Beyond potential revenue growth, ADVA Optical Networking’s focus on innovation and strategic technology partnerships will result in an expanding share of higher-margin, software-heavy applications as well as expanded service offerings, fueling our long-term profitability commitment. These opportunities will support our strategic focus to be the trusted partner for innovative connectivity solutions for existing and new customers. The combination of cost-effective innovation, short development and delivery times, a broad and growing customer base and well-balanced distribution model differentiates ADVA Optical Networking from its peers and will further fuel our sustainable business model for the benefit of our customers, shareholders and employees. I would like to thank our dedicated employees for their consistent and valuable contributions. Their combined talents have made ADVA Optical Networking a strong company with bright prospects for the future. Thank you! ADVA Optical Networking will continue to ***ADVANCE*** by ***capitalizing on next-generation networks.***

February 20, 2014

Brian Protiva
Chief Executive Officer

Supervisory Board

How Can Mobile Networks Deliver More?

Mobile network operators are about to face some of the biggest challenges in their history. Increasing the density of radio base stations is only one part of the equation when building 4G networks. Exact alignment between them is the other. This is why we care about precise timing delivery and assurance. We make sure that next-generation mobile broadband solutions deliver the experience the customer expects.

Members

ADVA Optical Networking's Supervisory Board consists of a diverse and international group of seasoned experts in their respective fields:

Anthony Maher, since 2002
Chairman

Chairman of the Compensation and Nomination Committee
Member of the Audit Committee

Managing Director, Belmondo Capital, Inc.,
Munich, Germany

Johanna Hey, since 2011
Vice Chairwoman

Chairwoman of the Audit Committee

Professor for tax law, University of Cologne,
Cologne, Germany

Eric Protiva, since 1999

Member of the Compensation and Nomination Committee

Managing Director, EGORA Holding GmbH,
Martinsried/Munich, Germany

Report to Shareholders

In 2013, the Supervisory Board once again performed its duties under the law and the Company's articles. It carefully and continuously monitored the Management Board and supported it in all strategic matters. The Supervisory Board has been directly involved in the early stages of all important strategic decisions of the Company. During a total of seven meetings (six ordinary meetings and one extraordinary meeting), in which the members of the Management Board regularly participated, the Management Board consistently, promptly and extensively informed the Supervisory Board about the business situation of the Company and the Group, in particular about strategic orientation, market development, prospects for growth and the development of net assets, financial position and profitability, including budgeting, investments, personnel, compliance, internal audit and risk management. The Supervisory Board extensively discussed all important business issues on the basis of the Management Board's reports. Any deviations of the actual business development from the Company's plans and objectives were explained by the Management Board in detail and reviewed by the Supervisory Board. The Supervisory Board gave its approvals to all important decisions, after thorough examination and consultation, where required by law or the Company's articles, acting in the best interest of the Company and Group. In addition to the seven meetings, but only on an exceptional basis, the Supervisory Board passed resolutions on urgent matters. Moreover, especially the Chairman and the Vice Chairwoman maintained regular contact with individual members of the Management Board outside of scheduled meetings and were kept up-to-date with respect to current business developments, important transactions and forthcoming decisions.

Main Management Board Activities Covered and Examined by the Supervisory Board
In 2013, as in the prior year, the Supervisory Board focused mainly on the business development and strategic direction of the Company and the Group, particularly its revenue, earnings and headcount development, and ADVA Optical Networking's financial situation. In this context, the consequences of the volatile revenue development were discussed.

The Supervisory Board closely monitored and supported the activities of the Management Board, including discussions on mergers and acquisitions, and approved the the liquidation of the Company's branch office in Saudi Arabia. It discussed the Group's organization and key business processes with the Management Board and assured itself of the efficiency of this organization and these processes. The Management Board submitted to the Supervisory Board all transactions and decisions requiring approval according to the Company's articles. The Supervisory Board approved all such transactions and decisions.

Committees
In order to perform its tasks efficiently, the Supervisory Board maintained two committees during 2013, the Audit Committee and the Compensation and Nomination Committee. Members of the Audit Committee were Johanna Hey (Chairwoman) and Anthony Maher, and members of the Compensation and Nomination Committee were Anthony Maher (Chairman) and Eric Protiva.

The Audit Committee held five meetings during the course of the year. In addition to reviewing the consolidated annual and three quarterly financial statements and Group management reports as well as the Company's annual financial statements and management report, the Audit Committee discussed the financial position and performance of the Group, the appointment of the external auditor, the audit scope for 2013, the development of tax positions and risks, internal audit activities, as well as the effectiveness of the internal controls related to financial reporting and of the risk management system.

The Compensation and Nomination Committee met four times during the past year. The Committee's discussions focused in particular on the remuneration of the Chief Officers.

Reports on the work of the Supervisory Board committees were regularly presented and discussed during the subsequent Supervisory Board plenary meeting.

Corporate Governance Code
The Supervisory Board welcomes the German Corporate Governance Code and supports its objectives. The Supervisory Board has approved compliance with and the implementation of most recommendations and proposals of the Corporate Governance Code within the ADVA Optical Networking organization. In its meeting on December 2, 2013, the Supervisory Board and the Management Board discussed the implementation of the Code, and jointly approved an updated declaration of compliance in accordance with section 161 of the German Stock Corporation Law (Aktiengesetz, AktG). This declaration is published on the Group's website and is accessible for all shareholders.

Annual Financial Statements and Management Reports
ADVA Optical Networking's consolidated annual financial statements for the year ended December 31, 2013, and ADVA Optical Networking SE's annual financial statements for the year ended December 31, 2013, as well as the Group management report and the management report of ADVA Optical Networking SE for the fiscal year 2013 were audited by the Company's appointed auditor for 2013, PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, Munich, who issued unqualified audit opinions. Pursuant to section 315a of the German Commercial Code (Handelsgesetzbuch, HGB), the consolidated annual financial statements have been prepared according to International Financial Reporting Standards (IFRS) as enacted in

the EU. All management letter points from the auditor were taken up, discussed with the Management Board, and their consideration was ensured.

All auditing materials and reports were submitted to the Supervisory Board members prior to the meeting of the Supervisory Board dealing with the Company's and Group's 2013 financial statements. On February 14 and 17, 2014, these materials were discussed and examined in detail jointly by the Audit Committee and the auditor and in consideration of the auditor's long-form report. The Audit Committee reported its findings to the entire Supervisory Board in its meeting on February 18, 2014. Furthermore, the auditor, who was present in all three meetings, reported on the material results of the audit, explained net assets, the financial position and the results of operations of the Company and the Group, and was available to answer additional questions from the members of the Supervisory Board.

In view and consideration of these audit reports and on the basis of the additional information provided by the auditor, the Supervisory Board discussed and examined the financial statements and management reports in detail in its meeting on February 18, 2014. It unanimously approved ADVA Optical Networking SE's annual financial statements and management report, as well as ADVA Optical Networking's consolidated annual financial statements and Group management report. The annual financial statements of ADVA Optical Networking SE for the fiscal year 2013 are thereby adopted.

Changes within the Management and Supervisory Boards

As of March 31, 2013, Christian Unterberger, Chief Sales & Marketing Officer, left ADVA Optical Networking by mutual agreement. He was instrumental in driving revenues through a comprehensive and proactive global program, determining product positioning and market launch strategies, as well as promoting ADVA Optical Networking's global brand identity. The Supervisory Board thanks Christian Unterberger for his valued contributions. His areas of responsibility have been assumed by Chief Executive Officer Brian Protiva. With this, the number of members of ADVA Optical Networking's Management Board has been reduced from four to three.

In its April 23, 2013 meeting, the Supervisory Board extended the appointment of Brian Protiva, Christoph Glingener and Jaswir Singh as members of the Management Board until December 31, 2014. Corresponding individual provisions were agreed to in writing.

There have been no changes within the Supervisory Board in 2013.

The Supervisory Board would like to express its appreciation for the personal dedication, performance and the ongoing commitment of the Management Board and all employees of the Company and the Group during 2013.

February 18, 2014

On behalf of the Supervisory Board:

Anthony Maher

Anthony Maher
Chairman of the Supervisory Board

The ADVA Optical Networking Stock

Does Virtualization Add Value Outside Data Centers?

Virtualization can be found everywhere inside the data center. It increases the utilization of compute and storage resources and improves application performance. But high-end applications involve more than one data center – and the geographic separation between these data centers can be significant. With our partners IBM and Marist College, we unveiled a business continuity solution that enables administrators to rapidly move virtual machines and data to remote locations with the push of a button. Geared towards software-defined networks, the open source system is designed to improve service levels and minimize downtime during natural disasters or other emergencies.

Disappointing share price development in 2013

The price of ADVA Optical Networking's share decreased in 2013 from EUR 3.98 on December 31, 2012, to EUR 3.74 on December 31, 2013. This represents a decline of EUR 0.24, or 6.0%. In an overall improved market, the share considerably underperformed the broad Nasdaq Composite Index (+38%) and the TecDAX (+38% as well), the average for major technology stocks in the Frankfurt Stock Exchange's Prime Standard segment. The Company's share price also considerably underperformed a portfolio of telecommunications equipment peer group stocks[1] (+45%).

High free float

As of December 31, 2013, the Company's nominal share capital totaled EUR 48,022,827, an increase of EUR 200,175 since December 31, 2012. The higher share capital is fully attributable to the issuance of ordinary shares related to capital increases from conditional capital following the exercise of employee options and similar rights throughout 2013. As for the shareholder structure of ADVA Optical Networking, at the end of 2013 free float equaled 82.0%, including 1.3% of outstanding ADVA Optical Networking stock held directly by members of the Management and Supervisory Boards, while the Company's sole major shareholder EGORA Group held the remaining 18.0%. Compared to the end of 2012, free float increased by 0.1% points. During the year, the Company did not utilize the share buyback authorized at the Annual Shareholders' Meetings in June 2010 and May 2012.

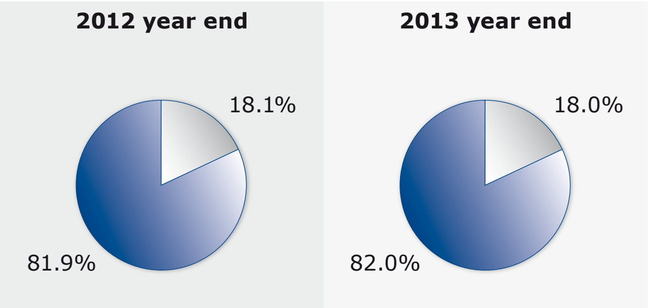
[1] Companies included in this portfolio are: Adtran, Brocade, Calix, Ciena, Cyan, Extreme Networks, Harmonic, Infinera, MRV Communications and Transmode. In addition, ADVA Optical Networking had included Tellabs in its list of peer group companies until December 3, 2013, the last day Tellabs' stock was publicly traded. As Tellabs was acquired by privately-owned Marlin Equity Partners in December 2013, however, at year-end 2013 the company was not part of this list anymore.

Stock Information[2]

Trade name	ISIN DE0005103006/ WKN 510300
Symbol	ADV
Exchange	Prime Standard Segment, TecDAX Frankfurt Stock Exchange
Sector	Technology
Industry	Communications Technology
Number of shares outstanding at year-end 2013	48,022,827
2013 high/low price	EUR 4.83/EUR 3.57
2013 year-end price	EUR 3.74
2013 year-end market capitalization	EUR 179.6 million
2012 year-end price	EUR 3.98
2013 share price performance	**-6.0%**

[2] Price information is based on Xetra closing prices.

Shareholder Structure



Shares outstanding	
47,822,652	48,022,827

● Free float ○ EGORA Group

Significant positive returns for global equity markets

Global equity markets posted significant positive returns in 2013. On a local currency basis, the MSCI World Index IMI rose by 24% in 2013 following an increase of 14% in the prior year. The year saw most of the developed market indices record their strongest performance in six years, driven by the easing of the EUR zone crisis, softer monetary policies and strong economic growth, while emerging market indices recorded negative returns, due to worries over potential economic imbalances resulting from cuts in global monetary stimulus. The MSCI index values rose by 31% in the U.S. and by 20% in Europe. Within Europe, MSCI index returns at the upper end were +39%, +30% and +25% for Ireland, Finland, and Denmark, respectively, and at the lower end came in at +7%, +15% and +16% for Austria, Portugal and the United Kingdom, respectively. In the major Asian markets, 2013 MSCI index growth was as strong as +52% and +10% in Japan and Hong Kong while Singapore developed sideways. Emerging markets showed a rather contrary trend with flat or downward developments and the respective MSCI index up a mere 1% on a local currency basis for 2013. While Greece, Egypt and South Africa were the top performers with positive MSCI index returns amounting to +19%, +18% and +13%, respectively, stock markets in Peru, Colombia and Chile performed the worst, with MSCI index values down 32%, 17% and 17%, respectively.

Technology stocks developed above the overall market

In general, technology stocks tended to perform above the overall market. The Nasdaq Composite and the German TecDAX indices closed the year up 38% each.

ADVA Optical Networking's share price performance was disappointing in 2013

In 2013, ADVA Optical Networking's share price performance at -6.0% was in contrast to the positive performance in the prior year (+9.9%), with the development of the Company's stock price well below the returns of major technology stock indexes.

From its 2012 year-end level of EUR 3.98, the Company's share price increased to EUR 4.29 until the end of February 2013 with moderate volatility and sound average Xetra trading volumes of 223 thousand shares per day supporting this development. Although Q4 2012 and Q1 2013 results released on February 28 and April 25, respectively, both came in at the upper half of guidance, the Company's share price dropped to its low for the year of EUR 3.57 on April 29, 2013. This development was driven by outlook numbers provided by the Company which for both quarters clearly fell below market expectations; the sequential decline of revenues in both quarters related to short-term market weakness driven by adverse macro-economic conditions and temporary shifts in carrier investment priorities. Coupled with competitors signaling a similar slowing trend, telecommunications equipment stocks began losing momentum. This was also reflected in decreasing Xetra trading volumes for ADVA Optical Networking's stock, which on average were at 174 thousand shares per day between March and June 2013.

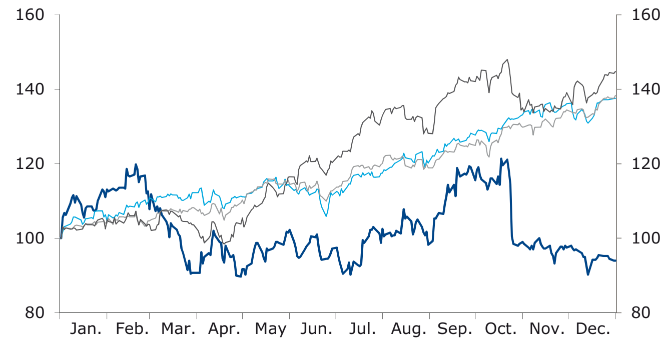
The Company released its Q2 2013 results on July 18, which were slightly above guidance, showed sequentially increasing revenues and included a record-high quarter-end cash position. ADVA Optical Networking's share price recovered nicely thereafter, and with the support of encouraging industry news, the Company's share price reached its 2013 peak on October 17 at EUR 4.83.

Although in line with guidance, the release of the Company's Q3 2013 results on October 24 disappointed the market once more, as ADVA Optical Networking guided Q4 2013 revenues sequentially down that day. While profitability was maintained in each quarter reported in 2013, a negative revenue trend driven by a challenging demand environment for telecommunications equipment solutions as well as slow demand from select major customers drove the Company's stock to price levels between EUR 3.59 and EUR 4.00 until the end of December. This lowered valuation levels once more, along with further reduced Xetra trading volumes of 146 thousand shares per day in H2 2013. ADVA Optical Networking ended 2013 with a share price of EUR 3.74 and a market valuation of EUR 180 million.

ADVA Optical Networking's valuation is low when compared to industry peer group companies

Compared to other listed telecommunication equipment peer group companies at year-end 2013, ADVA Optical Networking held an aggregate valuation at the lower end of the spectrum. Currently, as of February 12, 2014, ADVA Optical Networking has reached a market capitalization of EUR 183.9 million at a share price of EUR 3.83, above year-end 2013 levels. The valuation gap vs. the Company's peer group shows a significant discount on the basis of the enterprise value/sales ratio for 2014. ADVA Optical Networking believes that successful operating performance and growth will be reflected in more appropriate valuation levels going forward.

Price Development 2013 in Comparison (in %, indexed)



- ADVA Optical Networking
- TecDAX
- Peer group*
- Nasdaq Composite

* Peer group data are calculated with the arithmetic average of Adtran, Brocade, Calix, Ciena, Cyan, Extreme Networks, Harmonic, Infinera, MRV Communications, Tellabs and Transmode stock prices. Tellabs data is only included until December 3, 2013, the last day Tellabs' stock was publicly traded.

Investor Relations Review and Financial Calendar

What is at the Core of a Next-Generation Data Center?

The continued explosion in bandwidth demand is driving enterprises to evolve their high-density server virtualization, cloud architectures and storage applications. Gen 5 Fibre Channel (FC) technologies from our partner Brocade sit at the core of these next-generation data centers – and our 16G FC card is the first in the networking industry to achieve Brocade Gen 5 qualification. Our FSP 3000 sets the standard for data transport in tomorrow's data centers.

Key determining factors for ADVA Optical Networking's investor relations focus in 2013 were:

- Moderate market growth, volatile revenue development and sustained profitability
- Ongoing financial strength and operational flexibility
- Increased share of above-average margin enterprise networks business

Investor relations activities were maintained at a reasonable level

In a challenging macro-economic environment with temporary shifts in carrier investment priorities, short-term market weakness and volatile order volume from select major customers drove lower financial community interest in learning about ADVA Optical Networking than in previous years. Thus, the Company reduced its investor relations activities in 2013. The Company completed a total of five roadshows (2012: 19) in London, Frankfurt am Main, and Edinburgh, held more than 90 one-on-one meetings (2012: more than 200), and participated in a total of seven investor conferences (2012: 15). Of these, four were cross-sector conferences and three were technology-focused events; all of these conferences targeted institutional investors. These events were hosted by Baader Bank, Berenberg, Close Brothers Seydler Bank, Commerzbank, Deutsche Bank, Goldman Sachs, Kepler Cheuvreux and UniCredit.

Annual Analyst and Investor Day held

ADVA Optical Networking hosted its annual Analyst and Investor Day in September 2013 in London with all members of the Management Board present. In addition, with a total of 29 press releases, one ad hoc release, quarterly reports and regular conference calls, the financial community was kept informed about any significant developments within ADVA Optical Networking. Further, throughout the year, the Company continued to provide comprehensive and up-to-date information relevant to the financial community on the investor relations pages of its website at www.advaoptical.com, including full transcripts of archived conference calls.

At the end of 2013, seven financial analysts (end of 2012: eight) provided research coverage of ADVA Optical Networking's stock.

Financial Analyst Coverage

(as of December 31, 2013)

Institution	Financial Analyst Name	Location
Arete Research Services	Alban Cousin	London, United Kingdom
Berenberg	Ali Farid Khwaja	London, United Kingdom
Close Brothers Seydler Research	Veysel Taze	Frankfurt am Main, Germany
Deutsche Bank	Benjamin Kohnke	Frankfurt am Main, Germany
Edison Investment Research	Bridie Barrett Schmidt	London, United Kingdom
Hauck & Aufhaeuser	Tim Wunderlich	Hamburg, Germany
LBBW	Mirko Maier	Stuttgart, Germany

Overall trading liquidity in ADVA Optical Networking's shares decreased in 2013, driven by the volatile macro-economic environment, weaker than expected investments in telecommunications equipment and changes in institutional investor structure and focus. The average Xetra trading volume was at 168 thousand shares per day during 2013 after 219 thousand shares per day during the prior year. Free float in the Company's shares remained high in 2013, at levels between 81% and 82% throughout the year.

Continued high free float

Successful Annual Shareholders' Meeting

The Annual Shareholders' Meeting took place on June 4, 2013, in Meiningen, Germany. All items on the agenda were approved by a majority, including the creation of new authorized capital 2013/I with authorization to exclude subscription rights, the creation of additional contingent capital, and an extension of the authorization to issue share option rights. Further, several amendments to the articles of associations obtained approval (section 3: notices, section 8: composition of the Supervisory Board, section 9: term of office of the Supervisory Board). In addition, the variable remuneration of the Supervisory Board for 2012 as well as the appointment of PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft as the auditors for the 2013 financial results was approved.

Meeting the highest standards of open and transparent capital market communication is a key priority

Capital market communication in Germany is based on a broad range of frequently amended legal provisions, as for example enacted in the German Stock Corporation Law (Aktiengesetz, AktG) or the German Securities Trading Law (Wertpapier-Handelsgesetz, WpHG). As a Prime Standard company on the Frankfurt Stock Exchange, ADVA Optical Networking has continuously met the highest standards for open and transparent communication since its initial public offering in 1999. Therefore, the Company welcomes all regulations that provide enhanced standards of transparency and publication for shareholders. Compliance and implementation of these regulations, as with the German Corporate Governance Code, is continuously supervised by ADVA Optical Networking's legal department.

Financial Calendar

Publication of Three-Month Report 2014	April 24, 2014 Martinsried / Munich, Germany
Annual Shareholders' Meeting	June 5, 2014 Meiningen, Germany
Publication of Six-Month Report 2014	July 24, 2014 Martinsried / Munich, Germany
Publication of Nine-Month Report 2014	October 23, 2014 Martinsried / Munich, Germany

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Business Overview

Can We Bridge the Digital Divide?

The Internet has changed the way we communicate, how we share information, how we interact with our friends. But how do we make sure that no one is left behind? NoaNet is helping to close the digital divide in Washington State and push Internet access to more and more people. We are committed to helping NoaNet take this even further. With our Agile Core Express solution we helped them build a data highway that delivers an abundance of bandwidth for everyone.

Mission

Trusted supplier of next-generation data transport solutions

ADVA Optical Networking enables next-generation networks. The Company's mission is to be the trusted partner for innovative connectivity solutions that *ADVANCE* next-generation networks for cloud and mobile services.

Technology

ADVA Optical Networking develops, manufactures and sells transport solutions for next-generation telecommunication networks. The Company's products are based on fiber-optic transmission technology combined with Ethernet functionality (Optical+Ethernet) and intelligent software.

Optical

Multiplication of fiber capacity with Wavelength Division Multiplexing technology (WDM)

Fiber is the optimum physical medium to transmit large amounts of data over long distances. The bandwidth-over-distance capabilities of fiber by far exceed those of any other physical medium such as copper or wireless technologies. Therefore, fiber-optic transport is the unchallenged foundation for all high-speed networks. ADVA Optical Networking's optical transmission solutions are based on Wavelength Division Multiplexing (WDM) technology. With WDM, multiple data streams are transmitted simultaneously over a single optical fiber by assigning each stream to a different wavelength. Every wavelength (up to 192 in total) can carry a different application such as voice, video, data or storage traffic. Combining (i.e., multiplexing) these wavelengths at one end of the fiber, transmitting them over distance and then separating (i.e., de-multiplexing) them at the far end multiplies the fiber capacity and makes transmission more efficient. WDM supports all data protocols and transmission speeds, and is a natural foundation for all high-capacity networks.

Ethernet

Ethernet is the dominant data-link protocol for advanced networks

Ethernet is the dominant data-link protocol for today's networks supporting a multitude of communication applications. ADVA Optical Networking provides Ethernet-optimized transmission solutions for fiber-based networks used to interconnect enterprises and mobile network base stations with carrier networks. Ethernet is also one of the key protocols used to carry applications in high-speed optical networks for data backhaul and the interconnection of routers (see "Optical" above).

Automated Optical+Ethernet

Optical+Ethernet and intelligent software = foundation for high-speed networks

The combination of fiber-optic transmission technology and Ethernet-optimized data processing (Optical+Ethernet) is an ideal solution to deliver high-speed connectivity for data, storage, voice and video applications. Network operation is automated by an intelligent management software suite, which enhances the end-user experience and simplifies network operations.

ADVA Optical Networking creates Optical+Ethernet connectivity solutions from inception through manufacturing and into service. The following paragraphs describe important market dynamics that drive growth for the Company's business.

Market and Growth Drivers

Growth is driven by three market areas largely independent from one another

ADVA Optical Networking's market encompasses data networking solutions based on optical WDM technology and Ethernet transport and aggregation technology. Within this market, the Company covers three areas with distinct and largely independent growth drivers: carrier infrastructure, Carrier Ethernet access and dedicated enterprise networks.

Innovative products add value to and remove cost from customer networks

With innovative products, ADVA Optical Networking enables carriers and enterprises to deliver intelligent services, simplify their networks and scale their infrastructure for future growth. The Company's market-leading approach to combining Optical+Ethernet technologies with intelligent software into one integrated family of products provides a compelling value proposition to network operators looking for greater service assurance, automated network operation and expanded flexibility for a variety of services and topologies. Moreover, customers benefit from ADVA Optical Networking's powerful software and service-provisioning features that manage and control the entire network with lower costs and higher quality of service.

Carrier Infrastructure

Social media, video and cloud-based applications drive bandwidth demand

The largest driver for growth in the carrier infrastructure area of the market is the demand for social media, video streaming and cloud-based applications by private and business users.

Across the globe, this bandwidth demand is creating a surge in network traffic. Residential users demand faster access to the ever-increasing wealth of information on the Internet. In addition, they want broadband connectivity to exchange photos, watch videos or participate in online games and other bandwidth-intensive peer-to-peer applications. Video services (including video-on-demand, Internet television and video streaming) are the most popular applications in the residential market. This demand for high-quality video is forcing carriers to rapidly scale their networks to provision for intelligent triple play services (data, voice and video) and future growth. Business users have started to embrace cloud-based business solutions, requiring reliable, high-speed connectivity to their application hosting servers across high-performance carrier infrastructure.

A network upgrade for triple play services is not without challenges. Carriers have started delivering bandwidth in the range of several Mbit/s per household, aiming for 1Gbit/s in the near future. This is more than a factor of 10,000 higher compared to the bandwidth required for a traditional phone service and multiplies with the number of subscribers. Hence, at a network node that serves 100 households, which all subscribe to the new service, the carrier needs to handle 1,000,000 times the bandwidth.

Carriers use a wide range of access technologies

There are several ways for service providers to deliver broadband connectivity to their customers. Traditional telecommunications companies often rely on Digital Subscriber Line (DSL) technology to increase the capacity of their phone lines, i.e., twisted pairs of copper wires, which are typically available to every household. Coax cables are a good alternative, typically owned by cable TV companies that are expanding their offerings to become Multiple Service Operators (MSOs). New initiatives for Fiber-To-The-Home (FTTH) or Fiber-To-The-Building (FTTB) are rolling out, providing the ultimate bandwidth pipe. Last but not least, there are wireless technologies available, most well-known in the form of the Universal Mobile Telecommunications System (UMTS) – often referred to as third generation (3G) mobile technologies – and the current fourth generation (4G) mostly in the form of Long Term Evolution (LTE) standards, which all provide higher bandwidth per end user than legacy technology.

For carriers, the challenge is to provide good connectivity to as many customers as possible at the lowest possible cost. That means making good use of existing infrastructure, especially in the last mile, and intelligent investment in new technology to support growth and emerging applications. The trend toward flat-rate based pricing models, the rising cost of labor and other resources as well as the dramatic increase of end-user bandwidth require new and more powerful network concepts. The underlying network infrastructure needs to scale by many orders of magnitude and be simpler to operate, pushing fiber optic transmission technology closer to the end customer and making it the only viable choice for the backhaul and core of the network.

ADVA Optical Networking provides a unified access and backhaul solution for residential and business services

ADVA Optical Networking helps carriers to simplify their networks and build a scalable network infrastructure that is future-proof. With the Company's Optical+Ethernet product solutions, carriers can combine various traffic streams from different access technologies onto a single transport platform. Backhaul for copper, coax, fiber and wireless access technologies on a single platform eliminates the costly operation of parallel systems. In addition, ADVA Optical Networking offers one of the most scalable platforms on the market, allowing seamless transport from the customer premise to the core of the network. Thus, carriers can bypass some of the small access nodes, eliminating the expense of operating these locations.

More bandwidth to more customers from fewer network sites using less energy

The ability to deliver more bandwidth to more customers from fewer sites located farther back in the network enables operators to streamline their networks while simultaneously improving the end-user experience. Energy-hungry devices, which are needed for data processing, can be concentrated in fewer network locations, leading to a network architecture that is more energy-efficient and easier to operate.

Carrier Ethernet Access

Enterprises and mobile operators seek connectivity based on Ethernet

The key driver for growth in the Carrier Ethernet access area of ADVA Optical Networking's market is the migration from legacy technologies such as Synchronous Optical Network/Synchronous Digital Hierarchy (SONET/SDH) to intelligent and unified Ethernet-based transport and services, fueled by increased bandwidth demand from mobile data users and enterprises connected via fixed-line technology.

Mobile operators benefit from data-optimized high-speed backhauling

The success of high-speed mobile devices and services for private and business use has created a big opportunity for mobile operators – but also challenges for their networks. To launch and support these new data services, operators had to upgrade their mobile base stations to 3G and are now rolling out 4G (LTE) technology, with LTE-Advanced on the horizon. While both 3G and 4G technologies allow the delivery of more bandwidth over the air interface to the mobile device, operators also need to solve the backhaul challenge from the base stations to their core networks. Traditional backhaul was done via SONET/SDH leased lines or radio links. Higher-speed backhaul, however, needs to be data-optimized and relies to a large extent on fiber. In the context of 4G, mobile operators further increase the density of their cell sites, both, with macro and small cells. The higher density of antennae requires better synchronization between these cell sites. In summary, the build-out of mobile broadband networks leads to a new generation of fiber-based Carrier Ethernet solutions that deliver and assure high data throughput and accurate timing information.

Next generation mobile broadband requires accurate delivery and assurance of timing information

Enterprises want bandwidth, quality, performance and security

The drive for bandwidth is also reflected in the enterprise market where corporations seek high-speed connectivity between their geographically dispersed locations in order to exchange and store data more efficiently. Enterprises typically have two options when it comes to interconnecting their sites: they can build and operate a private network or rely on a managed service provider to give them the connectivity they need. Unlike residential customers, enterprises not only demand high bandwidth, but also have stringent requirements regarding quality of service, network performance, availability and security. Service providers can charge a premium for these attributes but need to back their service offerings with service level agreements.

Ethernet: from corporate Local Area Networks to carrier networks

Most enterprise networks today are based on Ethernet technology, which has established itself as the dominant data protocol for Local Area Networks (LANs). Ethernet was originally developed as a fair-access, open and ubiquitous connectivity protocol to interconnect computers within a single organization. The priorities here were low cost, ease of connecting/disconnecting from the network, fair allocation of best-effort bandwidth among all users and automatic discovery of resources on the network. The simplicity of the protocol, its packet-based nature similar to the Internet Protocol (IP) and its adaptability to new IP-based technologies has driven Ethernet's popularity in the enterprise market to the point where it is almost universally deployed. This popularity has driven volumes and reduced the cost of the basic technology blocks to very low levels.

ADVA Optical Networking has a market leading position for Carrier Ethernet access devices

The use of Ethernet in carrier networks requires modifications and enhancements to some of the original concepts since carriers are in the business of serving a wide range of customers from a common infrastructure platform. Carrier private services need to offer high security from intrusion or leakage of traffic between customers, isolation of faults on a customer's service from affecting others, access controls to ensure customers receive the service they paid for, quality of service guarantees and service level agreements. ADVA Optical Networking has built a market-leading position in Carrier Ethernet access devices, enabling carriers to deliver intelligent Ethernet services over any physical media, including fiber and copper. ADVA Optical Networking's unique Etherjack™ demarcation software provides unparalleled service assurance and Operations, Administration, Maintenance & Provisioning (OAM&P) capabilities that enable carriers to guarantee highest quality of service to their end users.

The strong popularity of Ethernet among enterprise users, the increasing demand from mobile operators for Ethernet-based connectivity to their base stations and the rapidly growing acceptance of Carrier Ethernet, combined with the typically lower cost of maintaining an Ethernet-based access network compared to running an access network based on legacy protocols such as Frame Relay and Asynchronous Transfer Mode (ATM) have paved the way for Carrier Ethernet to replace these incumbent technologies in the foreseeable future.

Enterprise Networks

Losing data is a threat to all companies and application downtime is costly

The key driver for growth in the enterprise network area of the market is the increasing need by enterprises to have a more reliable and efficient IT infrastructure that protects them against data loss. Loss of mission-critical information is, for many companies, a highly threatening scenario that could destroy or severely impact their business. In addition, more and more business transactions depend on the availability of electronic platforms. Application downtime results in revenue losses, idle staff and a damaged reputation for an enterprise.

Geographically dispersed storage networks provide maximum protection

While Ethernet services can solve the problem of high-bandwidth connectivity for corporate LANs between sites, enterprise CIOs are also increasingly concerned about the cost, security and availability of their business data. As a result, many large companies or research and education institutions are building or leasing their own private networks to provide greater control. In addition, financial institutions, insurance firms and other Fortune 1000 companies are generating mission-critical data at a rapid pace. Losing any data, not just mission-critical, puts an organization's future at risk, and application downtime is costly. These concerns are reinforced by regulatory demands such as Basel II/III and Sarbanes-Oxley legislation, ensuring that corporate attention will continue to be focused on data storage management. While Storage Area Networks (SANs) improve local corporate resource utilization and enable efficient management of rapidly-growing amounts of data at one particular site, a higher number of enterprises are seeking more comprehensive approaches to their data center management. Consolidation of storage resources to a number of different locations is the next step in storage management: enterprises achieve previously unknown levels of data availability and improve their cost and productivity positions, thanks to a geographically dispersed SAN setup. Optical WDM is the pre-eminent connectivity solution for enterprises wanting to implement high-performance distributed storage solutions that meet their needs for business continuity and data availability.

Private enterprise networks and cloud computing concepts require high-speed transport networks

As more and more business transactions depend on the availability of electronic platforms, an increasing number of industries (e.g., the health care, media and educational sectors) have found it economical to deploy or lease private enterprise networks. The emergence of mega data centers and new concepts for utility computing, cloud computing and server virtualization require more and improved high-speed transport networks. All these trends are enlarging the size of ADVA Optical Networking's target market.

Products

Optical+Ethernet = intelligence, simplicity, scalability

ADVA Optical Networking's portfolio strategy is built on a foundation of innovative Optical+Ethernet solutions that combine the strengths of the two core technologies with intelligent software into one unified family of products called the Fiber Service Platform (FSP). The Company uses this strategy to be the trusted partner in the Optical+Ethernet market, delivering next-generation connectivity solutions with intelligence, simplicity and scale, ultimately increasing the customers' service revenue potential and decreasing their total cost of ownership.

WDM provides maximum scalability

The optical expertise of ADVA Optical Networking is built on a core of WDM technology and is represented in the FSP 3000 platform. This technology enables the simultaneous transmission of independent applications across a common fiber infrastructure. By using separate wavelengths for different data streams, WDM multiplies the capacity of fiber cables. Network operators can leverage their existing fiber infrastructure for new applications and do more with fewer fibers to accommodate bandwidth growth.

Cloud services and data centers are accelerating the demand for WDM technology

With the accelerating trend to host data and applications in the cloud, data centers are becoming the new hot spots of fiber-optic networks. And consequently, high-speed connectivity for the rapidly increasing number of data centers drives the demand for more WDM technology. The FSP 3000 has a very successful track record of data center connectivity deployments and provides a highly differentiated feature set for this application.

FSP 3000: scalable optical transport

The FSP 3000 is a modular WDM system designed to maximize the bandwidth and service flexibility of access, metro and core networks. The unique optical layer design supports WDM-PON, CWDM and DWDM technology, including 100Gbit/s line speeds and colorless, directionless and contentionless ROADMs. RAYcontrol™, ADVA Optical Networking's industry-leading multi-layer GMPLS control plane, guarantees operational simplicity, even in complex meshed-network topologies. Thanks to Optical Transport Network (OTN), Ethernet and low-latency aggregation, the FSP 3000 represents a highly versatile and cost-effective solution for packet optical transport and data center interconnect. The platform opens new price performance points for cloud service providers.

FSP 3000 – The scalable optical transport solution

Ethernet provides the intelligence for innovative services

ADVA Optical Networking's Ethernet access solutions have been a core element of the Company's product portfolio since 2000, driven by the increasing demand for Ethernet services with carrier customers. With its FSP 150 family of products, ADVA Optical Networking has built a market-leading position in Ethernet access devices, enabling its customers to deliver intelligent Ethernet services over any physical media, including fiber and copper. The Company's unique Etherjack™ demarcation software provides unparalleled service assurance and OAM&P capabilities that enable carriers to guarantee highest quality of service to their end users.

Mobile broadband drives the demand for fiber-based Carrier Ethernet backhaul and accurate timing

More recently, mobile backhaul has emerged as one of the key applications for this product family. The sweeping success of smart phones and tablets creates an unprecedented demand for mobile broadband access. Mobile network operators respond with 4G technologies (LTE) and prepare for LTE-Advanced. In consequence, more and more base stations are being connected via fiber, and data-friendly Carrier Ethernet is the transmission technology of choice. The

FSP 150 portfolio provides significant value add in this application thanks to its capability to deliver and assure highly accurate timing information in addition to high data throughput.

FSP 150: intelligent Carrier Ethernet transport

The FSP 150 family of products provides devices for Carrier Ethernet service demarcation, extension and aggregation. It supports delivery of intelligent Ethernet services both in-region and out-of-region. Incorporating a Metro Ethernet Forum-certified user-to-network interface and the latest OAM and advanced Etherjack™ demarcation capabilities, the FSP 150 products enable delivery of service level agreement-based services with full end-to-end service assurance. Its comprehensive Syncjack™ technology for timing distribution, monitoring and timing service assurance opens new revenue opportunities from the delivery of synchronization services.

FSP 150 – The intelligent Carrier Ethernet transport solution

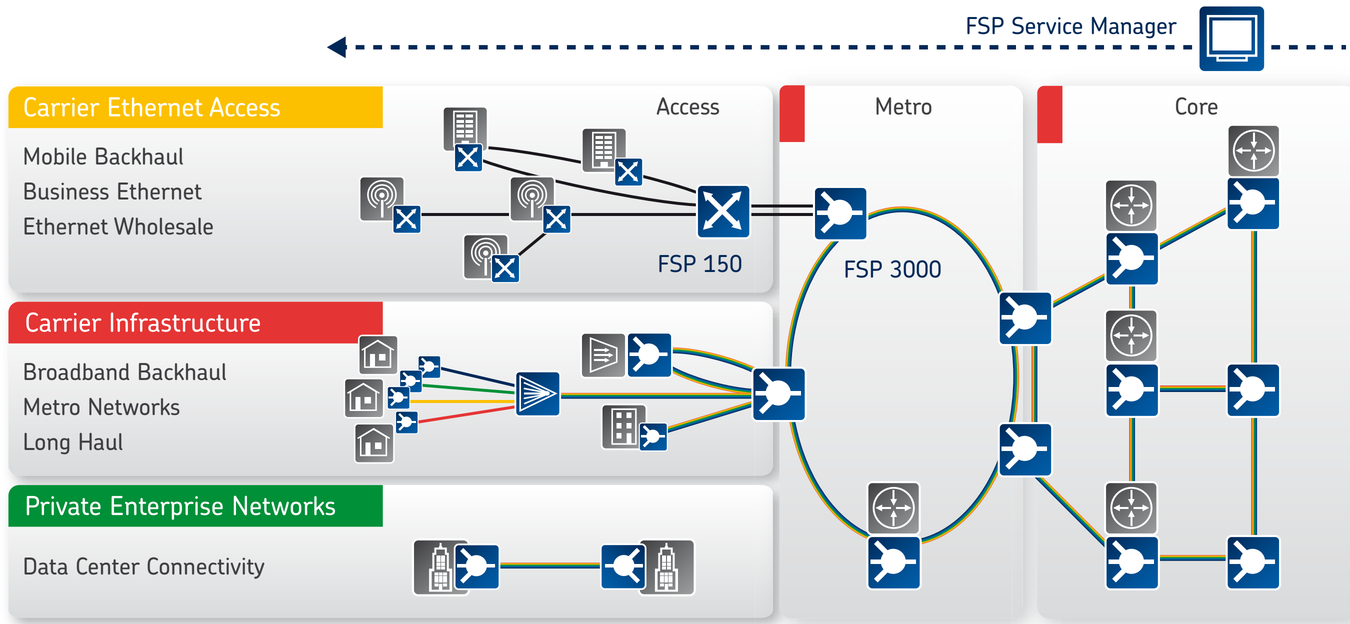
FSP Service Manager: complements hardware platforms, simplifies operations

Both hardware platforms, the FSP 3000 and FSP 150, are complemented by the FSP Service Manager, an enhanced component of the FSP Management Software Suite that simplifies the operation of end-to-end Optical+Ethernet networks. While the Company continues to add flexibility to its hardware platforms, ADVA Optical Networking also ensures that the additional functionality and associated degrees of freedom do not have a negative impact on the operator's user experience. The FSP Service Manager allows carriers to provision, turn up and maintain more services with less operational effort than ever before. They can take full advantage of new features without being burdened by lengthy and complicated operational processes.

FSP Management Software Suite reduces complexity and operational cost

ADVA Optical Networking's automated network management is built to reduce complexity and ultimately the cost of network operations. The FSP Management Software Suite provides a unified platform for network operations that empowers service providers and enterprise IT organizations to cost-effectively ensure availability and quality services. The FSP Management Software Suite is built on an intuitive graphical user interface that provides service provisioning and management across the entire network. With just a few simple mouse clicks, new services can be online, eliminating the need to drill down to configure individual elements.

The following image provides an overview of the application space for ADVA Optical Networking's Fiber Service Platform.



Support services: plan – build – care

In addition to hardware and software products, ADVA Optical Networking also offers a wide range of support services that help the Company's customers to plan, build and care for their networks.

Sales Regions and Customers

Diverse global customer base

ADVA Optical Networking sells its products to a broad customer base worldwide, either through distribution partners or its own direct sales force. In 2013, the Company continued to increase its global end-customer base with several wins with both carriers and enterprise customers across all regions. The evolution of the product portfolio further strengthened valuable relationships with British Telecom, Deutsche Telekom and other large carriers. The strength of ADVA Optical Networking's own sales team combined with the strength of select Value Added Resellers (VARs) was partially offset by an increasing uncertainty in the Original Equipment Manufacturer (OEMs) relationship with Coriant (former Nokia Siemens Networks' or NSN's fixed-line operations). Overall, in 2013 ADVA Optical Networking recorded revenues of EUR 310.7 million, down 5,9% from EUR 330.1 million in 2012.[1]

EMEA

EMEA is the largest sales region and shows continued growth potential

The region comprises Europe, Middle East and Africa.
Employees at year-end 2013: 937 (year-end 2012: 879)
Revenues in 2013: EUR 205.2 million (2012: EUR 199.3 million)

Customers in this region include AMS-IX, British Telecom, Cable & Wireless, COLT, DE-CIX, Deutsche Telekom, Media Broadcast, RomTelecom, Telecom Italia, Telefónica, Telia Sonera, Telkom South Africa and enterprise customers from the financial and other verticals. ADVA Optical Networking was able to withstand the continued macro-economic uncertainty caused by the EUR crisis and managed to expand its customer base. In a weak overall market environment, the Company was able to grow revenues in the EMEA region in 2013. EMEA continued to be the Company's largest sales region in 2013 and will continue to play a prominent role in the future.

In 2013, due to postponed carrier and enterprise investments, the market development in EMEA has been less favorable than in all other regions of the world. Catching up, an average market growth per year of 14%[2] is expected for this region through 2016. ADVA Optical Networking anticipates that the WDM market will continue to represent a major driver, as capacity is expanded to meet the rising business and residential demand for bandwidth in the access, metro and core of the network, further fueled by cloud services and data center growth. The market for Ethernet access solutions for enterprises also offers significant opportunity. In addition, the Company sees strong growth impulses through mobile backhaul projects. The upgrade of mobile networks to 4G LTE technology requires more fiber-based Carrier Ethernet access solutions in this space, and the preparation for LTE-Advanced drives the demand for the Company's synchronization solutions. Given the growth potential for WDM and Ethernet access, ADVA Optical Networking expects further positive development of its business in the EMEA region and strengthening of its market position.

Americas

Disappointing development in the Americas in 2013, return to sustainable growth in 2014

The Americas region comprises North America and South America.
Employees at year-end 2013: 322 (year-end 2012: 333)
Revenues in 2013: EUR 88.3 million (2012: EUR 112.6 million)

ADVA Optical Networking saw a significant revenue decline in the Americas in 2013. The Company had shown strong growth in Latin America in 2011 and was able to maintain a solid revenue flow in that sub-region in 2012. Due to political reasons, the 2012 level, however, could not be sustained in 2013. The North American business was driven by the tier 2 carrier market, the research and education vertical and some first success in the content service provider

[1] The split of total 2013 revenues of EUR 310.7 million is as follows:
- WDM product line FSP 3000: EUR 142.1 million,
- Ethernet access product line FSP 150: EUR 66.1 million, and
- other: EUR 102.5 million.

[2] Average annual industry analyst estimates 2013 to 2016 for metro and long-haul WDM equipment ("Optical") and Ethernet access devices ("Ethernet") relevant to ADVA Optical Networking. Sources: Infonetics Research Optical Network Hardware, Quarterly Market Share, Size, and Forecasts 3Q13, November 2013, and Infonetics Research Ethernet Access Devices Biannual Market Share, Size and Forecasts, 2nd Edition, September 2013.

space. The Company continues to maintain a broad customer base across the entire region and was successful in acquiring new business and accounts in all areas. Customers from this region include Cox Communications, Global Crossing, Level(3) Communications, NoaNet, NYSE Euronext, Telmex, Time Warner Cable, tw telecom and enterprise customers from the financial and other verticals.

The Company expects ongoing market growth in the Americas, amounting to an average of 11%[2] per year through 2016. Sales efforts are focused on servicing both carriers and corporate customers. Key corporate verticals are content service providers, Internet service providers, healthcare and financial institutions and federal and municipal governmental agencies. Growth in this region will be driven through demand for metro and regional carrier infrastructure deployments, enterprise applications, Ethernet access solutions for enterprises and mobile backhaul opportunities, for which ADVA Optical Networking is well-positioned. After the setbacks in 2013, ADVA Optical Networking expects to be back in growth mode in the Americas in 2014.

Asia-Pacific

The Asia-Pacific region comprises Australia, New Zealand, Greater China, India, Japan and South East Asia.
Employees at year-end 2013: 166 (year-end 2012: 166)
Revenues in 2013: EUR 17.2 million (2012: EUR 18.2 million)

Volatile revenue development in Asia-Pacific with continued growth expectations for the upcoming years

Due to the still relatively narrow customer base in the Asia-Pacific region, the development of respective revenues is still volatile. In 2013 ADVA Optical Networking saw decreasing revenue development in this region. There were mixed trends in the various sub regions, with some good demand from managed service providers and relatively weak demand for the Company's carrier infrastructure solutions. Customers in the Asia-Pacific region include KDDI, NextGen Networks, NTT, PCCW, SingTel, TATA Communications, Telstra, The Stock Exchange of Thailand and other enterprise customers from the financial and other verticals.

The region will also continue to develop positively, with an average annual market growth of 12%[2] through 2016. This development will primarily be driven by increasing managed service opportunities, more infrastructure deployments and Ethernet access business. The market conditions present good growth opportunities for ADVA Optical Networking and will be addressed through direct sales business and the further development of sales channel partnerships.

Sales and Marketing

Sales

Three-pronged sales distribution strategy

ADVA Optical Networking employs a direct-touch and proven three-pronged sales distribution strategy to maximize customer reach around the world:

- Direct sales,
- Sales through system integrators (i.e. Value Added Reseller partners or VARs), and
- Strategic partnerships with Original Equipment Manufacturers (OEMs).

Direct Sales

Direct sales is particularly important in the Ethernet access market and will be further expanded

The Company continues to focus on its direct-touch initiative as well as its direct sales force to win new customers. Establishing direct contact with enterprises and carriers enables ADVA Optical Networking to work more closely and better understand customers' specific requirements, which in turn helps to develop the right products and solutions. A direct sales approach is required in particular to address the evolutionary nature of the Ethernet access market. Due to the overall adverse development of its business, the Company closely managed its cost and did not make any significant changes to its sales headcount in 2013.

VAR Partners

VAR partners mostly provide access to carrier and large enterprise customers

VAR partners resell ADVA Optical Networking's products primarily under the brand name "ADVA Optical Networking" or with co-branded products under the name "Powered by ADVA Optical Networking". The Company works particularly closely with its distribution partners to provide planning and network consulting services for large enterprise and carrier customers and is intensely focused on developing optimized customer solutions. Partners typically provide the required technical support following network installation. In 2012, ADVA Optical Networking launched a new "Partner Ecosphere Program" (PEP), which provides distribution partners with in-depth training, fast and easy access to equipment and guarantees high-quality support. In 2013, several companies successfully passed the PEP certification and achieved "Select" or "Elite" status with more to come in 2014. VAR partners include Axians, Dacoso, Hewlett-Packard, Hitachi Data Systems, IBM, Infoguard, NEC, Sagem Télécommunications and Walker & Associates.

OEM Partners

OEM partners largely drive sales into incumbent carriers

OEM partners market, sell and support ADVA Optical Networking's products with extensive software and features integration into their own comprehensive portfolio. Main OEM partners are Coriant (former Nokia Siemens Networks' (NSN) fixed-line operations) and Fujitsu Network Communications (FNC). These channel partners generally have long and deep-rooted relationships with incumbent carriers and governmental agencies. They also sell ADVA Optical Networking's solutions with full integration into their network management platforms. Some incumbent carrier customers and select governmental agencies clearly value the OEM relationship to provide seamless new-product integration.

Marketing

Positioning of the "ADVA Optical Networking" brand

Direct-touch efforts are proactively supported by the marketing team to build the ADVA Optical Networking brand and to expand visibility of the FSP product portfolio. Specific marketing activities include regular participation in tradeshows and conferences, tactical online advertising, news coverage and bylined articles in trade publications. ADVA Optical Networking conducts customer and partner workshops, supports co-marketing efforts with its partners and delivers a quarterly e-newsletter to customers and partners. The Company also maintains a dynamic and active online presence, including a blog and social media outreach on multiple platforms. In 2013, ADVA Optical Networking exhibited at the Mobile World Congress tradeshow in Barcelona, Spain, at the Broadband World Forum Europe in Amsterdam, the Netherlands, at Communicasia in Singapore, Africacom in Cape Town, South Africa, Futurecom in Rio de Janeiro, Brazil, and at the OFC/NFOEC as well as at Comptel events in the USA. In addition to these major events, ADVA Optical Networking also participated in numerous smaller shows and organized customer events with targeted focus. To drive thought leadership, the Company continued strong relationships with industry trade press and analysts, delivered presentations at conferences and launched special event campaigns.

Focus on "Innovation", "Speed" and "Trusted Partner"

External communication was focused on "Innovation", "Speed" and "Trusted Partner". The combination of these three elements makes ADVA Optical Networking a unique player in the industry, combining R&D power and thought leadership with customer focus and personal touch. The brand promise underscores the Company's drive to help customers accelerate their transition to next-generation networks.

The product portfolio value proposition: intelligence, simplicity, scalability

ADVA Optical Networking's external marketing activities are targeted toward carriers that offer high-speed communication services and the enterprise customers that buy them. The Company continues to lead the industry with advanced Ethernet access and optical functionality, including software-based automation and an increasingly popular service offering. The marketing messages underscore its innovative, industry-leading position in all areas. Messaging supporting ADVA Optical Networking's advanced infrastructure for the access, metro and core network continues to be shared with the Company's partners. Together, ADVA Optical Networking and its partners convey a strong value proposition to the marketplace about the intelligence, simplicity and scalability of the joint product portfolios.

Marketing alliances with additional network equipment providers

Furthermore, ADVA Optical Networking continues to actively support marketing alliances with other global communications hardware and software vendors like Brocade, Corning, IBM, Infovista, JDS Uniphase and Juniper Networks. The numerous interoperability tests conducted with partners carry significant weight, as they demonstrate the compatibility of the various systems and assure customers that ADVA Optical Networking's products seamlessly integrate and operate with the systems of its partners and the customers' existing IT infrastructures. ADVA Optical Networking's partners serve as multipliers for joint marketing programs. This drives new customer opportunities and strengthens the Company's sales efforts.

Operations

Five core functions: strategic sourcing, sales back office, supply chain management, manufacturing engineering, manufacturing

Focus on highest quality levels, short delivery times and low cost

ADVA Optical Networking's operations activities consist of five core functions: strategic sourcing, sales back office, supply chain management, manufacturing engineering, and production. The integration of these functions with the global sales, R&D and quality management departments is the foundation for the Company's proven ability to provide innovative Optical+Ethernet networking solutions at highest quality levels and product performance while maintaining short delivery and response times and the benefit of the lowest total cost of ownership for the customer. In order to ensure its competitive positioning in the long run, ADVA Optical Networking leverages the capacities of tier 1 contract manufacturers for standard board production steps and building Ethernet access devices.

Strategic sourcing: worldwide collaboration with a consolidated supplier base, minimizing total supply chain sourcing costs

The strategic sourcing team manages sourcing of direct and indirect materials as well as contract manufacturing. The team is committed to source worldwide from a consolidated supplier base and to minimize total supply chain sourcing costs. Strategic sourcing is deeply engaged in R&D projects (upstream sourcing) and, by means of a bi-annual negotiation process, also provides continued cost reductions for all materials used in volume production. Particular focus is paid to capitalizing on the fierce competition in the innovative market for optical components, on using low-cost suppliers for mechanical components through a dedicated team residing in China, and on leveraging the scale of the Company's tier 1 contract manufacturers to obtain competitive prices for standardized electronic components. Key suppliers are covered by a state-of-the-art supplier management process consisting of periodic audits and assessments, commodity strategies, supplier classification models, performance scorecards and quarterly business reviews.

Sales back office: customer focus teams maintain relationships with established customers and develop strategies to maximize revenue opportunities through standardized portfolio usage

ADVA Optical Networking's sales back office consists of several customer focus teams (CFTs), each one dedicated to one territorial sales team. The CFTs maintain effective relationships with established customers and develop strategies to maximize revenue opportunities through standardized portfolio usage. They dynamically connect customer requirements to ADVA Optical Networking's internal planning and fulfillment processes, interact with other internal departments such as customer service and perform all related transactional order processing and accounting tasks. The CFTs also provide the sales management team with accurate reporting of all aspects of customer order processing, including weekly and monthly sales forecasts, the status of the sales pipeline, and the results of prospecting activities.

Supply chain management: high-quality and cost-efficient customer order fulfillment

The supply chain management (SCM) team is responsible for customer order fulfillment, including material and capacity planning, supply of components and shipment of finished goods. Furthermore, the SCM team drives global inventory and supplier management. Integrated SCM ensures the high-quality and cost-efficient manufacturing of build-to-order, even customer-specific WDM solutions with short delivery times, as well as the production of off-the-shelf and medium- and higher-volume Ethernet access solutions. Key priorities are the seamless execution of the sales & operations planning process and the implementation of advanced logistic models with the Company's suppliers. These processes lead to lower in-house inventory and working capital needs and at the same time to higher flexibility and customer service quality.

Manufacturing engineering: operations support and interface between development and manufacturing

ADVA Optical Networking's manufacturing engineering team drives the new product introduction process and provides technical support for in-house production as well as contract manufacturing operations. The team works closely with the Company's research and development engineers, applies a commonly approved industrialization process and collaborates with all development sites and manufacturing lines during the entire product lifecycle.

Manufacturing: combination of in-house production and outsourcing

ADVA Optical Networking has developed a unique and balanced manufacturing strategy combining the best from both outsourcing and in-house production. The Company's target is to maximize technology adoption, maintain high flexibility and minimize costs. The center of ADVA Optical Networking's internal manufacturing organization is a purpose-built 9,000 square meter facility in Meiningen, Germany. The transparent, glass-walled and award-winning building reflects the transparent order fulfillment process. This production setup provides a convincing answer to the ever-increasing demand for customized and flexible manufacturing with many short-term change requests, particularly those in WDM projects. Compared to fully contracted manufacturing, this approach ensures a major advantage in this key phase of the customer order fulfillment process with significantly increased flexibility and drastically shortened lead times for the benefit of the Company's customers.

Outsourcing of non-core manufacturing activities to the Company's tier 1 contract manufacturing suppliers ensures an efficient and flexible utilization of ADVA Optical Networking's own production resources as well as virtually unlimited access to manufacturing capacity. The main outsourcing partners leverage cost advantages for ADVA Optical Networking in low-cost regions such as Eastern Europe and China. The Company performs sophisticated and capital-intensive functional testing in-house, especially when it comes to customized complex system assembly, as the related processes are strategically relevant. ADVA Optical Networking has obtained TL 9000 certification for all its manufacturing facilities.

Major milestones reached in multi-year program for improving scale and efficiency until 2013

ADVA Optical Networking is currently engaged in a multi-year program aimed at improving scale and efficiency in manufacturing and distribution. The program aims to provide customers product configuration and distribution capabilities while at the same time minimizing overall manufacturing, procurement and freight network cost. Important milestones reached until 2013 were the following:

- Consolidation of all outsourced production activities with only two tier 1 electronic manufacturing service providers in Eastern Europe and in China.
- Start-up of an externally operated freight consolidation center within the free trade zone in Shenzhen in China.
- Setup of full product planning and configuration capabilities for the Company's main product lines into its distribution sites in York in the United Kingdom and Norcross, Georgia in the U.S.
- Augmentation of ADVA Optical Networking's enterprise resource planning system with multi-site planning capabilities and the centralization of supply chain management functions.
- Establishment of a supplier life cycle management system comprised of an integrated cost database, a multi-functional commodity management system and more stringent supplier on-boarding and supplier quality management processes.

Prestigious annual Supply Chain Management Award won in 2013

Significant improvements resulted from this program, both in terms of customer service (increased responsiveness and flexibility, reduced order lead times) and cost (higher administrational efficiency, lower inventory, reduced cost of goods sold, lower transportation cost). In June 2013, ADVA Optical announced that its transformation program had been recognized with the prestigious annual Supply Chain Management Award, presented by the management consulting unit of PricewaterhouseCoopers and the trade journal Logistik Heute, in partnership with the Institute for Supply Chain Management and the House of Logistics and Mobility.

Flexible organization and efficient cost structure

With this strong customer focus, flexible global organization and an efficient cost structure, ADVA Optical Networking has all prerequisites in place to support further successful development of its business.

Engineering

Unique organizational set-up, enabling fastest time-to market in the industry

ADVA Optical Networking's engineering organization is a unique and global organization which combines world-leading creativity with best-in-class realization teams in order to create differentiated product offerings. Maximum proximity to strategic customers and suppliers coupled with an efficient global product creation platform enable ADVA Optical Networking's position as a trusted technology partner with the fastest time-to-market in the industry. Major engineering locations are Shenzhen in China, Berlin and Meiningen in Germany, Oslo in Norway, Gdynia in Poland, Ra'anana/Tel Aviv in Israel and Richardson (Texas), Washington D.C. and Norcross (Georgia) in the U.S. In 2013, ADVA Optical Networking has further scaled its engineering activities by 9% to a total of 651 employees at year-end 2013 while optimizing the over-all set-up which will be further streamlined in 2014.

Innovative research, early prototypes, standardization activities as well as intellectual property rights management are driven by dedicated advanced technology groups. As an example for 2013, ADVA Optical Networking has been first to market and extended its leadership in the area of Software-Defined Networking (SDN) applied on optical solutions. Another key research area is around leading access and backhaul solutions from timing and synchronization over passive optical solutions to Network Functions Virtualization (NFV). Based upon this research and early prototypes, and taking into account input from strategic customers, ADVA Optical Networking's product line and lifecycle management teams define product and feature targets which are developed and tested by product engineering teams in a unique, agile and iterative way. The new product introduction team introduces these developments to manufacturing and enables the targeted volume production with highest quality.

Enhancement of scalable optical access and connectivity FSP 3000 solution

In 2013, the scalable optical transport solution FSP 3000 was enhanced by additional unique high-speed offerings around 100Gbit/s transmission, scalable switching and access solutions based on optical and electrical technologies (OTN and Ethernet) and a simplified management solution. With these additions, the FSP 3000 further manifests its leadership for service provider solutions ranging from access over metro to core as well as enterprise solutions covering data center connectivity and offerings for dedicated verticals like finance, media and health care. In 2014, ADVA Optical Networking intends to further enhance this leadership by developing cost-efficient connectivity solutions utilizing channel speeds above 100Gbit/s, extend the unique security offering by high-speed encryption solutions and unique access monitoring as well as optical solutions for mobile fronthaul and backhaul applications.

Additions to FSP 150 Ethernet transport family for wholesale business services and mobile backhaul

The FSP 150 Carrier Ethernet transport family for wholesale business services and mobile backhaul was extended by multiple additions throughout 2013. These include dedicated new family members around 1G Ethernet and 10G Ethernet offerings as well as family-wide introduction of enhanced availability/protection schemes and the further enhancement of the unique Syncjack™ suite combining synchronization and backhaul solutions for mobile infrastructure. In 2014, ADVA Optical Networking intends to expand the FSP 150 range towards higher speeds and extend the mobile backhaul offerings.

Evolution of software solutions

2013 has seen the further evolution of ADVA Optical Networking's SDN and management software with many industry-first demonstrations and realizations aimed at providing a platform for simple and easy-to-use deployment and handling of all the solutions ADVA Optical Networking offers. In 2014, a unified approach for all of ADVA Optical Networking hardware solutions will be introduced which enables existing and future customers to migrate towards application-oriented networking.

Quality Management

Main goal: customer satisfaction

Integration of quality management in all activities, from R&D to post-sales

Quality management is inherent to all ADVA Optical Networking business processes. The main goal of quality management is to understand and to meet, and wherever possible exceed, customer requirements. This is the basis for all research & development, operations and sales & marketing activities, in order to assure sustainable high quality levels and maximum customer satisfaction. The focus on quality management is crucial to maintain the Company's trusted partner reputation with customers, and it enables ADVA Optical Networking to remain a quality leader in its marketplace.

An annual customer satisfaction survey of ADVA Optical Networking's processes, products and services results in comprehensive feedback, which the Company uses as an important basis for continuous improvements. In addition to revenues and pro forma operating income, customer satisfaction, as measured by this survey feedback, represents an additional component in determining the variable compensation for members of the Management Board and the Company's second level of management. The quality management department reports directly to the chief executive officer. It acts as an overarching Group-wide advisory function, helping to uncover and eliminate weaknesses in all areas and processes within the Company. This results in high customer satisfaction ratings and greater efficiency. For 2013, ADVA Optical Networking's Net Promoter Score[3] was at +21%. While this is a strong result, the score is still down from +29% in 2012. Analysis suggests that in many cases ratings from 2012 detractors improved, while select 2012 promoters gave lower ratings in 2013. The Company will work with its customers in order to take appropriate measures to further improve customer satisfaction in 2014.

Strong Net Promoter Score in 2013, lower than in the prior year however

[3] The Net Promoter Score is obtained by asking customers a single question on a 0 to 10 rating scale: "How likely is it that you would recommend our company to a friend or colleague?" Based on their responses, customers are categorized into one of three groups: promoters (9–10 rating), passives (7–8 rating), and detractors (0–6 rating). The percentage of detractors is then subtracted from the percentage of promoters to obtain a Net Promoter Score.

Successful quality management starts in product engineering. It is therefore also an integral part of all ADVA Optical Networking development projects, starting with the product identification phase. The Company systematically analyzes failure rates over all phases of the development and product origination process, and from there derives corresponding optimization measures. This ensures high quality standards and product reliability.

With regard to operations activities, supplier quality is an important quality management component at ADVA Optical Networking. Thorough supplier selection and qualification, periodic evaluation by means of system and process audits and systematic inspection of incoming goods assures compliance with minimum quality requirements and fosters continued optimization. This is also supported by cross-functional commodity teams and the ever increasing involvement of the Company's suppliers in the development process.

Beyond standard quality gates and systematic testing during production, ADVA Optical Networking applies the staging concept to prepare its products for customer-specific installation. This concept is another important contributor to quality assurance. In order to provide maximum reliability, test configurations, settings and critical values are determined specific to each application.

Finally, ADVA Optical Networking optimizes its global processes, products and services by continuously improving its data analysis methods and tools across all functional areas. This ongoing optimization is essential to manage the complexity of the Company's wide-spread global activities, providing the basis for further growth. With the aim to identify weaknesses and opportunities in order to optimize cross-functional processes, ADVA Optical Networking has built an "efficiency engine" team and a project office as a systematic continuous improvement approach based on Lean Six Sigma methodologies. Beyond working towards the Company's strategic goal of operational excellence, the "efficiency engine" team is also tasked to identify and to drive projects key to the implementation of ADVA Optical Networking's other strategic goals of profitable growth, Optical+Ethernet innovation and employee development.

Sustainable resolutions create trust

In case of unexpected complaints after service deployment, ADVA Optical Networking strives to help its customers in quick and non-bureaucratic ways. The Company assesses the risk resulting from failures by means of standardized methods. It then analyzes the failures and their root causes and takes the appropriate corrective and preventive actions, with the goal to achieve sustainable resolutions for its customers

Successful TL 9000 5.0 and ISO 14001 repeat certifications in 2013

ADVA Optical Networking's focus on quality management shows in its successful 2013 repeat certifications in accordance with the renowned telecommunications quality and general environmental management practices TL 9000 5.0 and ISO 14001.

Group Management Report

Global Interworking – Who Moves All the Data?

We live in an era of mass collaboration, an era of sharing data, resources and knowledge, an era defined by global interworking. This trend will continue to increase and will continue to demand a supporting network that can transport enormous volumes of data. Research and education organizations are acutely aware of this. They are at the forefront of pushing boundaries. Together with the University of Michigan and our partner Juniper Networks, we showcased the future of big data transport. A global network based on a seamless interworking of optical layer and supercore routing technology. This isn't just a vision, it's a reality.

Forward-Looking Statements

This Group management report of ADVA Optical Networking SE contains forward-looking statements using words such as "believes", "anticipates" and "expects" to describe expected revenues and earnings, anticipated demand for optical networking solutions, internal estimates and liquidity. These forward-looking statements are based on the beliefs of the Management Board and respective assumptions made, and involve a number of unknown risks, uncertainties and other factors, many of which are beyond ADVA Optical Networking's control. If one or more of these uncertainties or risks materializes, or if the underlying assumptions of the Management Board prove incorrect, actual results can differ materially from those described in or inferred from forward-looking statements and information. Unknown risks and uncertainties are discussed in the "risk report" section further below.

In the following, ADVA Optical Networking SE as a company is labeled "the Company" or "ADVA Optical Networking SE", "ADVA Optical Networking" or "the Group" always refers to the ADVA Optical Networking Group.

Basis of Preparation

This Group Management Report of ADVA Optical Networking SE was prepared in accordance with sections 315 and 315a of the German Commercial Code (Handelsgesetzbuch, HGB) and German Accounting Standards (Deutsche Rechnungslegungs-Standards) No. 17 and 20 (DRS 17 and 20).

All information contained in this report relates to the status on December 31, 2013, or the financial year ending on that date, unless stated otherwise.

Strategy and Control Design

ADVA Optical Networking's strategic goals are profitable growth, innovation, operational excellence and employee development. The strategic goals are reviewed by both the Management Board and the Supervisory Board on a yearly basis and amended where appropriate. Each of these goals is defined in detail and then broken down into specific departmental and individual targets. The strategic goals are traced to each individual employee, so that each employee can focus and be evaluated on his/her individual performance and contribution to ADVA Optical Networking's overall performance.

ADVA Optical Networking measures the accomplishment of its strategic goals against revenues, pro forma operating income[1], net liquidity[2] and as a non-financial criterion customer satisfaction as measured by the Net Promoter Score[3]. These metrics represent the Group's key performance indicators. The Management Board sets target values for all four metrics for the year to come and measures actual values against the target values on a monthly basis for revenues and pro forma operating income, on a quarterly basis for net liquidity and on a yearly basis for the Net Promoter Score. In case of deviations from plan, corrective action can be taken quickly. This information is summarized and communicated to the Management Board in monthly, quarterly and yearly reports.

Revenues, pro forma operating income, net liquidity and Net Promoter Score operationalize strategic goals and represent ADVA Optical Networking's key performance indicators

[1] Pro forma operating income is calculated prior to non-cash charges related to the stock compensation programs and amortization and impairment of goodwill and acquisition-related intangible assets.

[2] Net liquidity is calculated by subtracting current and non-current financial liabilities as well as current and non-current finance lease obligations from cash and cash equivalents.

[3] The Net Promoter Score is obtained by asking customers a single question on a 0 to 10 rating scale: "How likely is it that you would recommend our company to a friend or colleague?" Based on their responses, customers are categorized into one of three groups: promoters (9–10 rating), passives (7–8 rating), and detractors (0–6 rating). The percentage of detractors is then subtracted from the percentage of promoters to obtain a Net Promoter Score.

General Economic and Market Conditions

Global economic growth about flat at a moderate 2.1% in 2013

The Global Economy in 2013 [4]

Overall, global economic growth was sluggish in 2013, five years after the onset of the global financial crisis. Global real gross domestic product rose by 2.1% in 2013 after an increase of 2.2% in the prior year. Among the high-income nations, the countries of the European Union overall continued to be plagued by high unemployment, wage compression, and low consumer confidence, leading to slowed growth, most pronounced by weaker private domestic demand. In part, this trend was offset by steady foreign trade. Developing countries remain the driver of global growth, and contrary to the European Union, growth was driven by domestic consumption, resulting from faster wage growth. The real gross domestic product of these countries rose by 4.7% (2012: 4.6%), largely due to strong growth rates in China (+7.6%, compared to +7.8% in 2012) and India (+5.2%, compared to +3.8% in 2012). The combined economies of high-income nations grew their real gross domestic product by a moderate 1.0% in 2013 (2012: 1.4%), mostly due to the consolidation of the banking sector and the continuing high unemployment rates. Within this group, the U.S. rose by 1.7% (2012: 2.2%), while the United Kingdom gained 1.1% (2012: 0.2%). The EUR countries, with significant variations among member states, declined by an overall 0.7% (2012: declined by 0.6%), with Germany rising by 0.3% (2012: rising by 0.7%) and Italy shrinking by 1.8% (2012: shrinking by 2.4%). Japan rose by 1.9% (2012: 1.9%), largely driven by a strong fiscal stimulus combined with monetary policy expansion to revive economic growth.

[4] Source: United Nations Conference for Trade and Development, September 2013. The 2013 numbers are preliminary.

Global Economic Prospects [5]

2014 growth expected at higher levels than in 2013, with global economy expanding by 3.2%

Global real gross domestic product is projected to grow by 3.2% in 2014, an increase from growth levels in 2013. At a projected 2.2%, growth in high-income countries should be below the global growth rate again for 2014, driven by reduced monetary stimulus and weak domestic demand. At an estimated real gross domestic product increase of 5.3%, the developing countries will once again drive global economic growth in 2014, based on increasing exports as well as strong trade and financial links with high-income economies. Spurred by strong domestic demand, with real gross domestic product growth rates of 7.7% and 6.2%, respectively, China and India are forecasted to remain the major contributors to growth in the developing countries in 2014.

Market Environment for ADVA Optical Networking

Optical+Ethernet market relevant for ADVA Optical Networking grew 12% in 2013

Average addressable market growth of 12% per year expected through 2016

In the volatile economic environment faced in 2013, the overall market for communications equipment suppliers relevant to ADVA Optical Networking showed 12% growth compared to the prior year.[6] Demand for Ethernet access devices developed slightly more favorably than for carrier infrastructure and enterprise networks. From a regional perspective, the market in the Americas and in Asia-Pacific grew significantly faster than in Europe, Middle East and Africa (EMEA). Industry analysts project that the communications equipment market relevant to ADVA Optical Networking will continue to show similar growth rates in 2014 and beyond, however with a more balanced regional distribution.

ADVA Optical Networking predominantly focuses on the segment for networking solutions based on fiber-optic transmission technology and Carrier Ethernet data transport

[5] Source: World Bank, Global Economic Prospects, January 2014.

[6] Industry analyst estimates for metro and long-haul WDM equipment ("Optical") and Ethernet access devices ("Ethernet") relevant to ADVA Optical Networking. Sources: Infonetics Research Optical Network Hardware, Quarterly Market Share, Size, and Forecasts 3Q13, November 2013, and Infonetics Research Ethernet Access Devices Biannual Market Share, Size and Forecasts, 2nd Edition, September 2013. The split of the WDM equipment into carrier infrastructure and enterprise solutions is based on ADVA Optical Networking internal estimates.

(Optical+Ethernet). The Group's addressable market is split into three areas: enterprise networks, carrier infrastructure and Carrier Ethernet access. The volume of ADVA Optical Networking's relevant market segment amounted to USD 9,598 million[6] (EUR 7,230 million[7]) in 2013. Of this total volume, "Optical" accounted for USD 8,843 million[6] (EUR 6,661 million[7]), while "Ethernet" contributed USD 755 million[6] (EUR 569 million[7]).

The growth of the overall market is primarily driven by steadily increasing bandwidth demand for wireless and wireline communication from residential end users and enterprises, with carriers continuously investing in new networking infrastructure solutions. Carrier decisions to substantially increase coverage and access capabilities of residential triple play services (data, voice and video) as well as the accelerated move to 4G wireless technology were major drivers for many next-generation network infrastructure builds. Data storage, cloud applications, the convergence of enterprise networks and the virtualization of storage and compute applications across multiple data centers have been the main drivers for enterprise connectivity. Furthermore, the Ethernet protocol has now evolved to be the standard carrier network protocol, replacing legacy protocols such as SONET/SDH, ATM and Frame Relay. Accordingly, between 2013 and 2016 the overall market for ADVA Optical Networking's Optical+Ethernet solutions is projected to grow by an annual average of 12%, accounting for a total of USD 13,401 million in 2016.[6]

10% of total market

Average addressable market growth of 13% per year expected through 2016

Market Environment for Enterprise Networks

The market for enterprise networks is approximately 10%[6] of the overall Optical+Ethernet market. Based on a volume of USD 979 million[6] (EUR 737 million[7]) in 2013, this market is expected to grow strongly at an average rate of 13%[6] per year until 2016. Increasing enterprise demand for high-bandwidth applications such as cloud computing and low-latency transmission, as well as continued outsourcing, fueled the market for managed services, interconnecting mega data centers and performance-assured access to data and resources hosted in the cloud.

82% of total market

Average addressable market growth of 12% per year expected through 2016

Market Environment for Carrier Infrastructure

The market for carrier infrastructure currently represents ADVA Optical Networking's most sizable opportunity. This area comprises 82%[6] of the Optical+Ethernet market. Based on a volume of USD 7,864 million[6] (EUR 5,924 million[7]) in 2013, carrier infrastructure solutions will grow by an average 12%[6] per year through 2016. ADVA Optical Networking expects that the significant growth in this area will be based primarily on expanding bandwidth demand from the carriers' residential and business customers. Expanding data traffic will continue to strain existing networks, thereby requiring carriers to further expand their infrastructure.

8% of total market

Average addressable market growth of 8% per year expected through 2016

Market Environment for Carrier Ethernet Access

ADVA Optical Networking traditionally holds a strong position in this market, which makes up 8%[6] of the Optical+Ethernet market. Based on a volume of USD 755 million[6] (EUR 569 million[7]) in 2013, this market is projected to grow at an average annual rate of 8%[6] until 2016. The growth will be driven by the continuous substitution of legacy services with intelligent and unified Ethernet services, fueled by increased bandwidth demand from enterprises and the upgrade of mobile backhaul solutions to accommodate the increasing bandwidth demand generated by the rollout of LTE and LTE-Advanced radio access technology. For ADVA Optical Networking, this market is an excellent opportunity to generate further revenue and profit growth through advancements in Ethernet technology.

[7] Calculated at the average exchange rate of USD 1.3276 per EUR in 2013.

Addressable market and growth rates [6]	2013 USD million	Share of total	CAGR* 2013-2016
Enterprise networks	979	10%	13%
Carrier infrastructure	7,864	82%	12%
Carrier Ethernet access	755	8%	8%
Total addressable Optical+Ethernet market	**9,598**	**100%**	**12%**

* CAGR = Compound annual growth rate.

Continuing strong market position

In its overall addressable market, ADVA Optical Networking continued to hold a strong position. For fiber-based Ethernet access devices, the Group ranks second with a market share of 18%.[8] For metro and long-haul optical transport solutions (enterprise networks and carrier infrastructure), ADVA Optical Networking remains a strong competitor in EMEA with a market share of more than 7%.[9]

[8] Based on 2012 total revenues for Ethernet access devices relevant for ADVA Optical Networking. Source: Infonetics Research Ethernet Access Devices Biannual Market Share, Size and Forecasts, 2nd Edition, September 2013.

[9] Based on 2012 total revenues for optical transport equipment relevant for ADVA Optical Networking. Source: Infonetics Research Optical Network Hardware, Quarterly Market Share, Size, and Forecasts 3Q13, November 2013.

Business Development and Operational Performance

Revenues

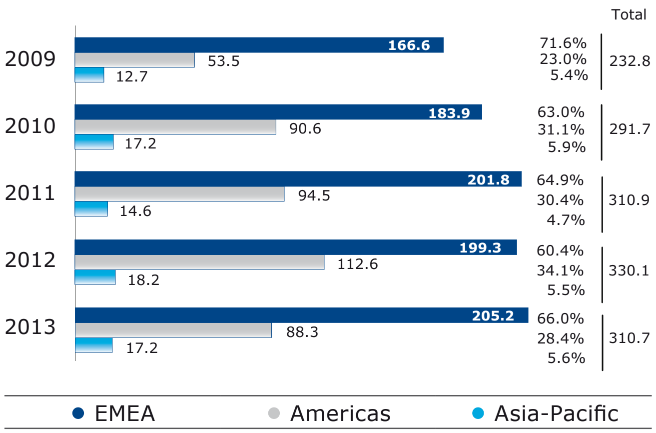
Revenue decrease in 2013

Revenues represent one of the four key performance indicators for ADVA Optical Networking. In 2013, the Group generated revenues of EUR 310.7 million, a decrease of 5.9% on revenues of EUR 330.1 million in 2012. This decline in revenues mainly relates to weaker short-term market demand for Ethernet access solutions from one of the Group's larger customers and general weakness in demand for carrier infrastructure solutions.

EMEA remains most important sales region, followed by the Americas and Asia-Pacific

The most important sales region in 2013 remained EMEA, followed by the Americas and Asia-Pacific. EMEA revenues were up 3.0% from EUR 199.3 million in 2012 to EUR 205.2 million in 2013, comprising 66.0% of total revenues in 2013, up from 60.4% in 2012. The improved revenues reflect a sound customer base in a mature market with many new customers adopting ADVA Optical Networking's technologies. In particular, demand for enterprise networks business rose significantly as EMEA customers continued to purchase the Group's 100G technology, directly as well as via managed services offered by carriers. In the Americas, revenues decreased significantly by 21.6% from EUR 112.6 million in 2012 to EUR 88.3 million in 2013, due to decreased Ethernet access and carrier infrastructure revenues. The corresponding share of total annual revenues decreased from 34.1% to 28.4%. In the Asia-Pacific region, revenues were down by 5.2% from EUR 18.2 million in 2012 to EUR 17.2 million in 2013, mainly related to high volatility due to relatively low levels of run rate business in this region, and temporarily lower carrier infrastructure business. The Asia-Pacific region comprised 5.6% of total revenues in 2013 after 5.5% in 2012. However, the region still continues to show new opportunities and growth potential. ADVA Optical Networking will continue to invest in growing its market share in the Americas and selective emerging markets.

Revenues by Region
(in millions of EUR and relative to total revenues)



Since ADVA Optical Networking is only active in a single operating segment, which is the development, production and marketing of optical networking solutions, a further breakdown of revenues is not relevant.

Results of Operations

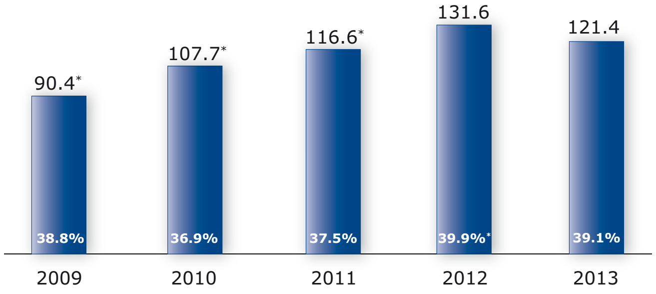
(in millions of EUR, except earnings per share)	2013	Portion of revenues	2012	Portion of revenues
Revenues	**310.7**	**100.0%**	**330.1**	**100.0%**
Cost of goods sold	-189.3	60.9%	-198.5	60.1%
Gross profit	**121.4**	**39.1%**	**131.6**	**39.9%**
Selling and marketing expenses	-47.1	15.2%	-46.8	14.2%
General and administrative expenses	-26.3	8.5%	-26.0	7.9%
Research and development expenses	-43.5	14.0%	-42.1	12.7%
Other operating income and expenses, net	2.5	0.8%	2.1	0.6%
Operating income	**7.0**	**2.2%**	**18.8**	**5.7%**
Interest income and expenses, net	-1.1	0.3%	-1.1	0.4%
Other financial gains and losses, net	-1.5	0.5%	0.8	0.3%
Income before tax	**4.4**	**1.4%**	**18.5**	**5.6%**
Income tax benefit (expense), net	1.1	0.4%	-1.8	0.5%
Net income	**5.5**	**1.8%**	**16.7**	**5.1%**
Earnings per share in EUR				
basic	0.11		0.35	
diluted	0.11		0.34	

Cost of goods sold decreased from EUR 198.5 million in 2012 to EUR 189.3 million in 2013, primarily due to the decline in revenues. Cost of goods sold includes amortization charges for capitalized development projects of EUR 17.8 million in 2013 after EUR 15.4 million in 2012.

Lower gross profit is mainly a result of lower revenues

Gross profit declined from EUR 131.6 million in 2012 to EUR 121.4 million in 2013, comprising 39.9% and 39.1% of revenues, respectively. The decrease in gross profit compared to the prior year is predominantly due to lower revenues. The development of the Group's gross margin is impacted by variations in regional revenue distribution and in product and customer mix.

Gross Profit
(in millions of EUR and relative to total revenues)

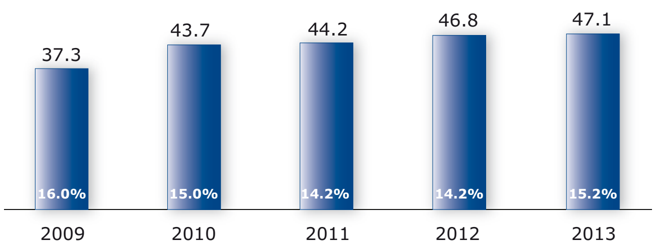


* From 2012, amortization for capitalized development projects is presented as cost of goods sold. Prior period information has been adjusted accordingly.

Selling and marketing expenses grew due to direct-touch sales activities and extended post-sales customer service

Selling and marketing expenses of EUR 47.1 million in 2013 were slightly up from EUR 46.8 million in 2012, and comprised 15.2% and 14.2% of revenues, respectively. The increase is largely driven by investment in post-sales customer service as well as in ADVA Optical Networking's intensified direct-touch activities with those key customers served via indirect distribution channels. Establishing direct contact enables the Group to work more closely with its end customers and better understand their specific requirements, which in turn helps in developing suitable products.

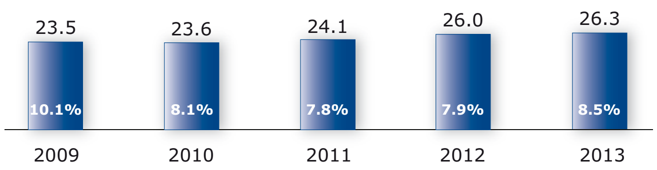
Selling and Marketing Expenses
(in millions of EUR and relative to total revenues)



General and administrative expenses slightly above prior year levels largely due to changes in ADVA Optical Networking's group structure

General and administrative expenses at EUR 26.3 million in 2013 were slightly up from EUR 26.0 million recorded in 2012. The share of total revenues increased from 7.9% in 2012 to 8.5% in 2013. This increase is mainly due to one-off expenses incurred on changes in ADVA Optical Networking's group structure. The percentage of revenues ratio is also impacted by lower revenues.

General and Administrative Expenses
(in millions of EUR and relative to total revenues)

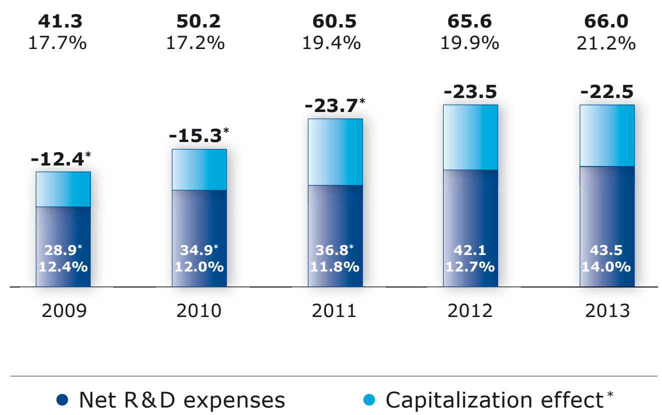


ADVA Optical Networking's research and development activities are driven by the distinct emphasis on differentiating its highly innovative Optical+Ethernet solutions and working with customers and partners to identify and meet their current and future needs. The resulting key technologies and products radically simplify complicated network structures and supplement existing solutions. During 2013, R&D activities focused on the development of the enhanced FSP 3000 platform.

Further increase in R&D expenses

At EUR 43.5 million in 2013, net R&D expenses were up from the EUR 42.1 million in 2012, thereby constituting 14.0% of revenues in 2013 after 12.7% in the prior year. The increase is due to further investment in advanced Optical+Ethernet technology and one-off personnel expenses. R&D expenses included income from capitalization of development expenses of EUR 22.5 million in 2013, down from EUR 23.5 million seen in 2012. The capitalization rate in 2013 amounted to 34.1% (prior year: 35.9%). The decrease is due to reduced capitalization of Ethernet solutions.

Research and Development Expenses
(in millions of EUR and relative to total revenues)



* From 2012, amortization for capitalized development projects is presented as cost of goods sold. Prior period information has been adjusted accordingly.

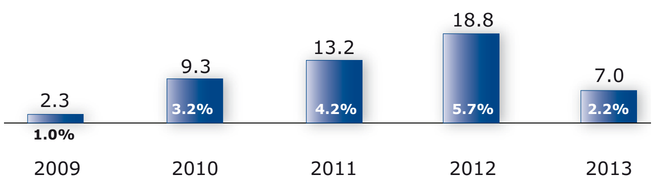
Net other operating income and expenses amounted to positive EUR 2.5 million in 2013, up from positive EUR 2.1 million in the prior year. This item is mainly impacted by subsidies received for specific research activities and release of provisions created in earlier periods.

Total operating expenses increased by EUR 1.6 million, from EUR 112.8 million in 2012 to EUR 114.4 million in 2013, representing 36.8% of revenues in 2013 after 34.2% in the prior year.

Significant decline of operating income

Overall, ADVA Optical Networking reported a significantly decreased operating income of EUR 7.0 million in 2013 after an operating income of EUR 18.8 million in the prior year. The decline in operating result is largely due to lower revenues and gross margin. Additionally, operating expenses increased due to one-off costs related to cost saving initiatives that were started in 2013 and that will take effect from 2014.

Operating Income
(in millions of EUR and relative to total revenues)

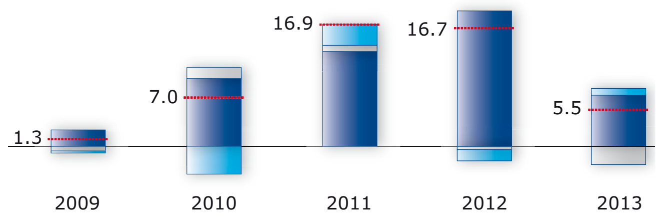


Net income is mainly driven by operating income and tax benefit

Given the unfavorable development of operating income, ADVA Optical Networking reported net income of EUR 5.5 million for 2013, after EUR 16.7 million in 2012. Beyond operating income, the net result in 2013 was driven by net interest expenses of EUR 1.1 million (prior year: EUR 1.1 million) and net other financial losses of EUR 1.5 million (prior year: net other financial gains of EUR 0.8 million) relating to the translation of foreign currency assets and liabilities and to gains and losses on hedging instruments.

In 2013 the Group reported an income tax benefit of EUR 1.1 million after an income tax expense of EUR 1.8 million in 2012. The 2013 tax benefit is mainly due to the release of tax provisions related to open tax audit appeals that have been partially resolved in 2013.

Net Income
(in millions of EUR)



Basic and diluted earnings per share were both EUR 0.11 in 2013 after EUR 0.35 and EUR 0.34 in the prior year. Basic average shares outstanding increased by 0.3 million to 47.9 million in 2013, due to capital increases from the exercise of stock options. Diluted weighted average shares outstanding decreased by 0.2 million to 48.6 million in 2013.

Pro forma Operating Income
Pro forma operating income[1] represents one of the four key performance indicators for ADVA Optical Networking. This metric is derived from operating income as follows:

(in millions of EUR)	2013	2012
Operating income	**7.0**	**18.8**
Stock compensation expenses	+0.9	+1.4
Amortization of intangible assets from acquisitions	+0.7	+1.6
Pro forma operating income	**8.6**	**21.8**

As pro forma operating income excludes non-cash charges related to stock compensation and acquisitions, the Management Board of ADVA Optical Networking believes that pro forma operating income is the more appropriate measure than operating income when comparing the Group's operational performance with the operational performance of other telecommunications equipment providers.

Pro forma operating income decreased significantly

The decrease of pro forma operating income from EUR 21.8 million in 2012 to EUR 8.6 million in 2013 is mostly due to the reduction in operating income discussed further above.

Summary: Business Development and Operational Performance
Overall, the business development and operational performance in 2013 declined significantly when compared to 2012. This was predominantly a result of the unfavorable revenue development.

Net Assets and Financial Position

Total assets increased, proportion of non-current assets is slightly up

Balance Sheet Structure
ADVA Optical Networking's total assets increased by EUR 9.0 million or 3.2%, up from EUR 284.1 million at year-end 2012 to EUR 293.1 million at the end of 2013.

(on December 31, in millions of EUR)	2013	2012
Current assets	178.8	174.3
Non-current assets	114.3	109.8
Total assets	**293.1**	**284.1**
Current liabilities	71.9	91.7
Non-current liabilities	63.4	38.5
Stockholders' equity	157.8	153.9
Total equity and liabilities	**293.1**	**284.1**

Current assets rose by EUR 4.5 million or 2.6% from EUR 174.3 million on December 31, 2012 to EUR 178.8 million on December 31, 2013, and comprised 61.0% of the balance sheet total after 61.4% at the end of the prior year. The increase in current assets was mainly driven by a rise in cash and cash equivalents partly offset by lower trade accounts receivable and inventories. Cash and cash equivalents were up from EUR 70.6 million at year-end 2012 to EUR 80.9 million at the end of December 2013, resulting mainly from financing activities. At the same time, trade accounts receivable decreased by EUR 2.7 million to EUR 52.7 million mainly due to lower revenues. Days sales outstanding were at 64 days in 2013 after 59 days reported in 2012 mainly due to the granting of extended payment terms to few select customers. In addition, inventories of EUR 40.1 million at the end of 2013 were EUR 1.2 million lower than at the end of December 2012, with inventory turns at 4.6x in 2013 after 5.2x in 2012. Other current assets were down by EUR 1.8 million to EUR 5.0 million.

Non-current assets increased by EUR 4.5 million from EUR 109.8 million at year-end 2012 to EUR 114.3 million on December 31, 2013. Within non-current assets, capitalized development projects grew by EUR 4.6 million to EUR 52.1 million at year-end 2013. The increase was largely driven by enhancements to the FSP 3000 platform. In addition, deferred tax assets rose by EUR 2.5 million to EUR 15.0 million at year-end 2013, mainly related to the recognition of deferred tax assets on loss carry-forwards of ADVA Optical Networking SE. These effects were compensated in part by a decrease in property, plant and equipment by EUR 1.4 million to EUR 21.9 million at the end of 2013 and a decrease in other intangible assets by EUR 0.9 million to EUR 2.7 million, due to regular amortization charges and overall reduced investments.

Additional off-balance sheet assets

Meaningful additional assets belonging to ADVA Optical Networking are the broad and global customer base of several hundred service providers and thousands of enterprises, the ADVA Optical Networking brand, the vendor and partner relationships and a highly motivated and skilled global team. These assets are not included in the balance sheet. Customer satisfaction as measured by the Net Promoter Score[3] represents one of the Group's four key performance indicators, highlighting the value of sustainable relationships with customers to ADVA Optical Networking.

Total liabilities increased; lower current liabilities and higher non-current liabilities

With respect to equity and liabilities, current liabilities decreased by EUR 19.8 million from EUR 91.7 million at year-end 2012 to EUR 71.9 million at the end of 2013, primarily due to decreases in trade accounts payable and current financial liabilities. Trade accounts payable declined from EUR 38.1 million at the end of 2012 to EUR 26.5 million at year-end 2013, with days payable outstanding at 65 days in 2013 compared to 62 days in 2012. The decrease is mainly due to changes in purchasing volumes per individual supplier. Current financial liabilities were down by EUR 10.5 million to EUR 4.2 million, mainly affected by the repayment of a bonded loan of EUR 14.0 million. In addition, tax liabilities were reduced by EUR 2.9 million to EUR 2.0 million at the end of 2013 mainly due to the release of provisions for corporation tax in ADVA Optical Networking SE. Partly offsetting these effects is an increase in current provisions by EUR 3.0 million to EUR 8.2 million, largely due to costs related to saving initiatives started in 2013.

Non-current liabilities increased to EUR 63.4 million at December 31, 2013 after EUR 38.5 million at year-end 2012. Within non-current liabilities, non-current financial liabilities increased by EUR 20.7 million to EUR 35.0 million at the end of 2013 due to a new loan received in June 2013. Furthermore, deferred tax liabilities were up by EUR 4.1 million to EUR 18.3 million on December 31, 2013 based on temporary differences.

Higher stockholders' equity due to net income and capital increases related to exercise of stock options

Stockholders' equity increased by EUR 3.9 million from EUR 153.9 million at year-end 2012 to EUR 157.8 million at the end of 2013, mainly due to net income of EUR 5.5 million reported for 2013. In addition, capital increases totaling EUR 0.4 million from the exercise of stock options, and stock compensation expenses totaling EUR 0.2 million, were reported in 2013. The equity ratio was at 53.8% at the end of 2013, after 54.2% at year-end 2012. The non-current assets ratio amounted to 138.1% on December 31, 2013, with stockholders' equity fully covering the non-current assets and a portion of the current assets. This healthy balance sheet structure reflects the Group's careful financing strategy.

Balance sheet ratios (on December 31, in %)		**2013**	**2012**
Equity ratio	Stockholders' equity / Total assets	53.8	54.2
Non-current asset ratio	Stockholders' equity / Non-current assets	135.1	140.2
Liability structure	Current liabilities / Total liabilities	53.1	70.4

Capital Expenditures

Capital expenditures for additions to property, plant and equipment and finance leases in 2013 amounted to EUR 7.4 million, down from EUR 9.2 million in 2012, largely reflecting lower investments in production and test equipment.

Capital expenditures for property, plant and equipment are mainly related to investments in production & test equipment

Capital expenditures for intangible assets of EUR 23.2 million in 2013 were down from EUR 25.0 million in the prior year. This total consists of capitalized development projects of EUR 22.5 million in 2013 after EUR 23.5 million in 2012, and investments in software licenses and other intangible assets of EUR 0.7 million in 2013 after EUR 1.5 million in 2012. Investments in capitalized development projects are mainly driven by development activities for ADVA Optical Networking's enhanced FSP 3000 platform.

Capital expenditures for intangible assets are mainly related to capitalized development projects

Cash Flow

(in millions of EUR)	2013	Portion of cash	2012	Portion of cash
Operating cash flow	31.4	38.8%	45.2	64.0%
Investing cash flow	-29.9	37.0%	-34.8	49.3%
Financing cash flow	9.0	11.2%	-0.1	0.1%
Net effect of foreign currency translation on cash and cash equivalents	-0.2	0.3%	1.2	1.7%
Net change in cash and cash equivalents	**10.3**	**12.7%**	**11.5**	**16.3%**
Cash and cash equivalents at the beginning of the period	70.6	87.3%	59.1	83.7%
Cash and cash equivalents at the end of the period	**80.9**	**100.0%**	**70.6**	**100.0%**

Decreased operating cash flow mainly due to lower income before tax

Cash flow from operating activities at EUR 31.4 million in 2013 was down EUR 13.8 million from EUR 45.2 million in 2012. This development was largely due to the lower income before tax partly offset by higher non-cash relevant depreciation and amortization of tangible and intangible assets. Net cash required for working capital overall in 2013 increased by EUR 1.1 million compared to 2012.

Decreased use of funds for investing activities

Cash flow from investing activities was EUR -29.9 million in 2013 after EUR -34.8 million in the prior year. The decreased use of funds for investing activities is largely due to lower cash outflows for technical equipment and machinery as well as for capitalized development projects.

Positive financing cash flow

Finally, cash flow from financing activities at positive EUR 9.0 million in 2013 was significantly above the 2012 level at negative EUR 0.1 million. The 2013 cash flow from financing activities is largely due to the increase in financial liabilities related to a new loan cashed in June 2013, partly offset by the repayment of a bonded loan and the regular servicing of other existing debt.

Overall, including the net effect of foreign currency translation on cash and cash equivalents of EUR -0.2 million (2012: EUR 1.2 million), cash and cash equivalents rose by EUR 10.3 million in 2013, from EUR 70.6 million at year-end 2012 to EUR 80.9 million at the end of 2013, after an increase of EUR 11.5 million in the prior year.

Strong equity base

Financing and Liquidity

ADVA Optical Networking's financial management objective is to provide sufficient funds to ensure ongoing operations and to support the Group's projected growth. Beyond the strong equity base appropriate for the business, ADVA Optical Networking finances its business by means of liabilities with maturities typically exceeding the life of the assets being financed. For any liability taken, ADVA Optical Networking is focused on minimizing related interest cost, as long as access to funds is not at risk. Excess funds are used either to redeem debt or are invested in short-term interest-bearing term deposits.

Financial liabilities (on December 31, in millions of EUR)	**2013**	**2012**
Current financial liabilities	4.2	14.7
Non-current financial liabilities	35.0	14.3
Total financial liabilities	**39.2**	**29.0**

Higher financial liabilities

Total financial liabilities increased from EUR 29.0 million at year-end 2012 to EUR 39.2 million at the end of 2013. While the current portion decreased from EUR 14.7 million to EUR 4.2 million, the non-current portion increased from EUR 14.3 million on December 31, 2012, to EUR 35.0 million at the end of December 2013, mainly affected by the repayment of a EUR 14.0 million bonded loan classified as current and a new loan amounting to nominally EUR 25.0 million received in June 2013. The new loan has a 5 year maturity and a fixed interest rate of 2.55% per annum. The loan principal will be repaid in 16 equal installments of EUR 1,563 thousand per quarter commencing in Q3 2014. All financial liabilities were exclusively denominated in EUR at the end of 2012 and 2013.

The following table gives an overview on interest terms and the maturity structure of each financial liability at year-end 2013:

(in millions of EUR)	**Dec. 31, 2013**	**Interest terms**	**Maturity** ≤ 12 months	**Maturity** 12 – 36 months	**Maturity** > 36 months
IKB Deutsche Industriebank loans*	0.8**	Fixed rate, subsidized***	0.3	0.5	-
	2.1	Fixed rate, subsidized***	0.8	1.3	-
	24.9	Fixed rate, subsidized***	3.1	12.4	9.4
Portigon AG bonded loan*	11.4	Floating rate based on 3M EURIBOR	-	-	11.4
Total financial liabilities	**39.2**		**4.2**	**14.2**	**20.8**

* Key covenants refer to the Group's year-end debt/equity ratio and to the quarter-end net liquidity.

** The IKB Deutsche Industriebank loan is secured by a mortgage without certificate of EUR 5.6 million (prior year: EUR 5.6 million) on the production and development site in Meiningen, Germany.

*** Subsidized by the German Reconstruction Loan Company (Kreditanstalt für Wiederaufbau, KfW).

On December 31, 2013, the Group had available EUR 8.0 million (on December 31, 2012: EUR 8.0 million) of undrawn committed borrowing facilities in respect of which all conditions had been met.

Further details about the Group's financial liabilities can be found in note (13) to the consolidated financial statements.

Very strong net liquidity

Net liquidity represents one of the four key performance indicators for ADVA Optical Networking. Due to the increase in cash and cash equivalents and corresponding increase in financial liabilities in 2013, ADVA Optical Networking's net liquidity at EUR 41.7 million remained about stable compared to year-end 2012. Cash and cash equivalents of EUR 80.9 million on December 31, 2013, and of EUR 70.6 million on December 31, 2012, were invested mainly in EUR, USD and in GBP. At the end of 2013 and 2012, access to EUR 0.3 million and EUR 0.4 million of cash and cash equivalents was restricted, respectively.

Net liquidity (on December 31, in millions of EUR)	**2013**	**2012**
Cash and cash equivalents	80.9	70.6
- finance lease obligations		
current	-0.0	-0.0
non-current	-0.0	-0.0
- financial liabilities		
current	-4.2	-14.7
non-current	-35.0	-14.3
Net liquidity	**41.7**	**41.6**

ADVA Optical Networking's liquidity ratios reflect the healthy balance sheet structure of the Group.

Financing ratios (on December 31)		**2013**	**2012**
Cash ratio	$\frac{\text{Cash and cash equivalents}}{\text{Current liabilities}}$	1.13	0.77
Quick ratio	$\frac{\text{Monetary current assets}^{*}}{\text{Current liabilities}}$	1.86	1.38
Current ratio	$\frac{\text{Current assets}}{\text{Current liabilities}}$	2.49	1.90

* Monetary current assets are defined as the sum of cash and cash equivalents, short-term investments and securities and trade accounts receivable.

Reduction in return on capital employed due to lower operating income

Return on capital employed in 2013 was at 3.3%, considerably down from 10.0% in 2012. This unfavorable development is largely due to the decline of operating result reported in 2013.

Return on capital employed (ROCE) (base data in millions of EUR)		**2013**	**2012**
Operating income		7.0	18.8
Average total assets*		291.1	269.6
Average current liabilities*		81.3	80.9
ROCE	$\frac{\text{Operating income}}{\text{Ø total assets} - \text{Ø current liabilities}}$	**3.3%**	**10.0%**

* Arithmetic average of five quarterly period-end values (Dec. 31 of the prior year and Mar. 31, Jun. 30, Sep. 30 and Dec. 31 of the year).

Transactions with Related Parties
Transactions with related individuals and legal entities are discussed in notes (33) and (34) to the consolidated financial statements.

No dividend payments

Dividend Payments
In 2013 there were no dividend payments for 2012 (prior year: nil for 2011). ADVA Optical Networking does not plan to pay out a dividend for 2013.

Summary: Net Assets and Financial Position
The net assets and financial position of ADVA Optical Networking continues to be strong in 2013, with cash and cash equivalents at significantly higher levels than at year-end 2012 and net liquidity about unchanged.

Share Capital and Shareholder Structure

On December 31, 2013, ADVA Optical Networking SE had issued 48,022,827 no par value bearer shares (December 31, 2012: 47,822,652). No other class of shares had been issued during the reporting period.

Year-end free float at 82% about unchanged compared to the end of the prior year

At year-end 2013, EGORA Holding GmbH held a total of 8,656,749 shares or 18.0% of all ADVA Optical Networking SE shares outstanding (at year-end 2012: 8,656,749 shares or 18.1% of all shares outstanding). 6,330,902 of these shares or 13.2% of all shares outstanding (at year-end 2012: 6,330,902 shares or 13.2% of all shares outstanding) were held by EGORA Ventures GmbH, a 100% subsidiary of EGORA Holding GmbH, and the remaining 2,325,847 shares or 4.8% of all shares outstanding (at year-end 2012: 2,325,847 shares or 4.9% of all shares outstanding) were held directly by EGORA Holding GmbH. Both EGORA companies have their registered offices in Fraunhoferstrasse 22, 82152 Martinsried/Munich, Germany. No other shareholder has filed with the Company to have held more than 10% of the Company's shares outstanding on December 31, 2013. Further details on share capital and shareholder structure are disclosed in note (17) to the consolidated financial statements.

Restriction of Voting Rights and Share Transfers

At year-end 2013, the Management Board of ADVA Optical Networking SE had no knowledge of any restrictions related to voting rights or share transfers.

Appointment and Dismissal of Management Board Members

The appointment and dismissal of members of the Management Board of ADVA Optical Networking SE follows the direction of the German Stock Corporation Law (Aktiengesetz, AktG), the German SE Implementation Act (SE-Ausführungsgesetz, SEAG) as well as the provisions in section 6 of the Company's current articles of association, dated June 6, 2013. According to these articles, in principle the Supervisory Board appoints the members of the Management Board and does so for a maximum period of five years. However, it is the Company's practice to appoint the members of the Management Board for two years only. Repeated appointment is possible. The Management Board of ADVA Optical Networking SE regularly consists of two individuals. However, the Supervisory Board may appoint a higher number of individuals. If the Management Board consists of more than one individual, the Supervisory Board may appoint one member of the Management Board Chief Executive Officer or Speaker of the Management Board, and another member his or her deputy. The Supervisory Board may recall an already-effective appointment for important reasons. In 2013, the number of Management Board members was reduced from four to three. At the end of March 2013, Christian Unterberger, Chief Sales & Marketing Officer, left the Company by mutual agreement. His areas of responsibility have been assumed by Chief Executive Officer Brian Protiva. There were no additional appointments or dismissals of Management Board members. At the end of 2013, ADVA Optical Networking SE's Management Board consisted of Brian Protiva (Chief Executive Officer), Christoph Glingener (Chief Technology Officer) and Jaswir Singh (Chief Financial Officer & Chief Operating Officer).

Changes to Articles of Association

Changes to ADVA Optical Networking SE's articles of association follow section 179 of the German Stock Corporation Law (Aktiengesetz, AktG) in conjunction with section 133 AktG, as well as the provisions in section 4 paragraph 6 and section 13 paragraph 3 of the Company's current articles of association, dated June 6, 2013. Accordingly, in principle any changes to the articles of association need to be resolved by the Shareholders' Meeting. However, the Shareholders' Meeting has authorized the Supervisory Board to change the version of the articles of association in accordance with capital increases from authorized capital and conditional capital.

Issuance and Buy-Back of Shares

At year-end 2013:

Authorized capital at 49.8% of share capital

Conditional capital at 9.5% of share capital

Authorization to buy back shares of up to 9.6% of share capital

The rights of the Management Board to issue new shares are regulated in section 4 paragraphs 4 to 5k of the articles of association of ADVA Optical Networking SE. According to ADVA Optical Networking SE's current articles of association, last amended on June 6, 2013, the Management Board may issue up to 23,911,326 shares from authorized capital, amounting to a total of EUR 23,911,326 against cash or contribution in-kind with possible exclusion of subscription rights. On December 31, 2013, the authorized capital amounted to EUR 23,911,326, i.e., that day the Management Board may have issued up to 23,911,326 shares or 49.8% of total shares outstanding. In addition, on December 31, 2013, a total of two tranches of conditional capital amounting to a total of EUR 4,782,265 or 10.0% of the share capital were recorded in the commercial register. The conditional capital has been used for granting stock option and similar rights to members of the Management Board, to employees of the Company and to management and employees of affiliated companies. The conditional capital increase is put into effect only if and when the holders of the option rights exercise these rights. 200,175 new shares were already created in 2013 as a result of the exercise of stock options, but will only be registered in the trade register after the balance sheet date. Thus, the number of shares that can be issued by the Management Board from the two tranches of conditional capital is reduced to 4,582,090 or 9.5% of total shares outstanding.

At year-end 2013, the Management Board was authorized to buy back, until May 31, 2015, up to 4,600,000 own shares of the Company. This equals 9.6% of the share capital issued on December 31, 2013. This right was granted to the Management Board by a resolution of the Shareholders' Meeting on June 9, 2010 and amended by a resolution of the Shareholders' Meeting on May 24, 2012. Shares bought back may be used exclusively as compensation for the acquisition of companies, parts of companies or investments in companies, for issuing stock to employees of the Company or affiliated companies, for serving share subscription rights from the Company's stock option plans, and for redeeming the shares.

Takeover Bid-Driven Change of Control Provisions

At year-end 2013, a bonded loan with redemption value of nominally EUR 11.5 million (due in January 2017) and a loan with redemption value of nominally EUR 25.0 million (to be repaid in 16 equal quarterly installments from September 2014), respectively, are part of ADVA Optical Networking SE's financial liabilities. In the event of a potential takeover bid-driven change in control of ADVA Optical Networking SE, the creditors have the right to terminate these loans with immediate effect.

On December 31, 2013, for the event of a takeover bid-driven change in control there have been no recourse agreements in place with any of the members of the Management Board or with any of the Group's employees.

Employees, Social and Environmental Responsibility

Employees

On December 31, 2013, ADVA Optical Networking had 1,425 employees, including 13 apprentices. The breakdown of permanent employees by department is listed in the table below:

Employees per department (on December 31)	**2013**	**2012**	**Change**
Research and development	651	599	+52
Purchasing and production	199	205	-6
Quality management	21	21	+0
Sales, marketing and service	395	390	+5
Management and administration	146	146	+0
Apprentices	13	17	-4
Total employees	**1,425**	**1,378**	**+47**

On average, ADVA Optical Networking had 1,427 employees during 2013, up from 1,337 during 2012. Furthermore, there were 12 and 13 temporary employees working for ADVA Optical Networking at year end 2013 and 2012, respectively. During 2013, the increase in employees largely related to the acquisition of Biran High-Tech Advisors Ltd, Ra'anana/Tel Aviv, Israel (renamed to ADVA Optical Networking Israel Ltd.) in Q1 2013 which at the time brought 41 employees on board, mostly in the research & development area. The acquisition and the rise in total employees was driven by intensified Optical+Ethernet software development activities.

Total headcount increased, mostly related to the acquisition of Biran High-Tech Advisors, adding research & development resources

Employees per country (on December 31)	**2013**	**2012**	**Change**
Germany (including apprentices)	496	512	-16
USA	319	329	-10
Poland	223	193	+30
China	133	131	+2
United Kingdom	103	102	+1
Israel	45	-	+45
Norway	24	25	-1
France	16	15	+1
India	12	12	+0
Singapore	11	14	-3
Italy	8	9	-1
Other countries	35	36	-1
Total employees	**1,425**	**1,378**	**+47**

Personnel expenses increased from EUR 105.5 million in 2012 to EUR 112.8 million in 2013, representing 36.3% of revenues in 2013 compared to 32.0% in 2012.

Compensation comprises fixed and variable elements

ADVA Optical Networking successfully attracts and retains highly qualified staff due to its competitive compensation programs and the rewarding work environment offered. The employee compensation packages comprise fixed and variable elements, and also include stock options and/or stock appreciation rights. These compensation packages enable employees to participate appropriately in the success of the Group and support employee retention, while at the same time rewarding individual efforts, teamwork, innovation and productivity. Furthermore, employees who perform exceptionally well or who make suggestions for significant improvements are recognized through the Group's Spot Award program.

In addition, the Group is committed to offering all employees comprehensive on-the-job training, as well as specific continuing education opportunities in order to advance their personal and professional development.

Comprehensive education programs through the ADVA Optical Networking University

The Group offers three types of continuing education programs through the ADVA Optical Networking University, based on employee development needs. These needs are identified, documented and reviewed semi-annually within an electronic performance appraisal and competency management system:

1. Through ADVA Optical Networking's general development program, employees are offered courses on various topics that are regularly requested, including language classes, standard office software know-how and the improvement of communication, presentation, conflict management and project management skills.

2. ADVA Optical Networking offers specific training courses, partly online, tailored to meet individual employee needs. These courses also include technical training, which is mostly conducted internally by the Group's own technical experts.

3. ADVA Optical Networking has launched a global in-house management training program. This customized initiative is targeted at all leaders with people-management responsibilities. The Group offers a set of different courses according to experience and knowledge levels, which helps managers understand how to maximize both individual and team performance.

ADVA Optical Networking is convinced that these three components form a solid foundation from which the Group can utilize the skills of its employees and foster their continuing development.

Within ADVA Optical Networking, all relevant local regulations for health and safety in the workplace are complied with and for the Group's sites in some countries are regularly monitored by independent engineering offices for safety in the workplace. ADVA Optical Networking provides a global work environment that is clean, bright and friendly. An efficient employee representation without trade union ties is in place on a global basis, reflecting the international employee base and overall orientation of the Group.

Global employee representation

ADVA Optical Networking is an equal opportunity employer and has an on-going commitment to the creation of a workplace free of discrimination and harassment. The Group recruits, hires, trains and promotes individuals on all job levels without regard to race, religion, ancestry, sexual orientation, marital status, national origin, age, gender and physical or mental disability. ADVA Optical Networking is committed to a fair and equitable workplace where everyone is a respected and valued member of the team. The Group's core values (teamwork, execution, accountability and motivation) and leadership principles (integrity/honesty, decisiveness and respect) guide employees and managers in all business activities.

Equal opportunities for all employees

In order to ensure observance of all applicable laws and regulations, ADVA Optical Networking has a code of conduct and a range of Group-wide policies in place which govern the Group's business operations and are mandatory for all employees to follow. The code is an extension of the Group's core values, and employees are encouraged to report suspected incidents of non-compliance and to seek support when having questions or suggestions. An external ombudsman (this role is currently covered by Frank Fischer, tax lawyer and former member of ADVA Optical Networking's Supervisory Board) and an externally operated ethics and compliance helpline enable confidential and anonymous reporting. Enforcement of compliance with all applicable laws and regulations and deriving internal policies is coordinated by ADVA Optical Networking's Chief Compliance Officer who reports to the Chief Executive Officer and the Supervisory Board.

Comprehensive compliance system in place

At its main production and development facility in Meiningen, Germany, ADVA Optical Networking currently provides 13 apprenticeship positions, which lead to professions as electronic technicians for devices and systems and as office clerks. The Company is among the most recognized apprenticeship providers for industrial electronics professions in Southern Thuringia, the region in which this facility is located. In addition, ADVA Optical Networking offers an active university student trainee program in Germany that provides on-the-job work experience to students pursuing degrees.

Recognized apprenticeship positions

The Group relies on a team of highly qualified and motivated employees of 39 different nationalities, with extensive experience in telecommunications and in various other industries. The interdisciplinary and intercultural exchange among employees on all levels advances the open and transparent culture of the Group and the creativity of its employees in the best possible way. In 2013, the Group conducted an employee survey with the support of an independent human resources consultancy, with improved overall feedback compared to the last survey taken in 2011, which had already shown better results than the preceding survey from 2010. Based on the results of the 2013 survey, the Management Board derived an action plan to further improve employee satisfaction.

International, highly qualified and motivated employees

Social Responsibility

As for suppliers, ADVA Optical Networking treats them as an organizational extension and expects them to act as the Group expects its employees to act, with the highest standards for ethics and social responsibility. These expectations are defined in ADVA Optical Networking's supplier code of conduct, which is based on the widely-accepted Electronics Industry Citizenship Coalition (EICC) code of conduct. Each supplier needs to give confirmation of compliance with this code. Further, ADVA Optical Networking has implemented a supplier assessment process intended to uncover risks and address them. This process consists of a supplier survey that documents compliance on every term of the Group's supplier code of conduct, scoring in a risk assessment per-

Supplier evaluation driven by compliance with highest standards for ethics and social responsibility, based on the EICC code of conduct formed by the Group, and finally on-site supplier audits. In 2013, ADVA Optical Networking completed four such audits on key suppliers.

Social responsibility of the Group and its employees

Beyond its focus on employees and suppliers, ADVA Optical Networking is eager to help address the needs of the community, in particular to involve itself locally where it conducts business. Based on a broad range of activities, the Group maintained a global program in 2013 that focuses on the communities in all regions where ADVA Optical Networking is present. Seven global and 30 local project managers coordinated a total of 57 initiatives in 2013. Initiatives encompassed the following:

Sponsorships to local charities, communities and research programs; the Group subsidized runs and walks supporting

- disease research, relief and cure,
- orphans and other disadvantaged groups,
- the general awareness for the environment.

Employee collections and donations

- Money, blood, school supplies, toys, clothes, food and blankets.
- Volunteering time for caring for the elderly, cleaning up public places, making blankets for children and shelter animals, collecting and delivering toys, food and other goods.

Raising employees' awareness for the environment

- The Group has adopted a telecommuting policy that allows employees to save gas and support the environment.
- A recycling program is in place.
- Finally, ADVA Optical Networking promotes a low-carbon lifestyle by walking or riding a bicycle to work.

Environmental Responsibility

Actively caring for the environment is very important

Not actively taking care of the environment would have a negative impact to ADVA Optical Networking. Customers demand that the Group shows responsibility, and require evidence of efforts. Care for the environment is fully integrated in how ADVA Optical Networking does business.

Products consume little energy

When compared to the products of its competitors, the Group's platforms generally consume less energy, a fact customers have supported with statements confirming the positive overall energy balance of ADVA Optical Networking's platforms deployed in their networks.

Easy recyclability at the end of the product life cycle

The modular platform design allows simple upgrading and ensures that the products can be recycled easily at the end of the product life cycle. As a manufacturer of optical and electronic products, ADVA Optical Networking complies with the European Union's requirements, including the regulations on waste electrical and electronic equipment (WEEE), on the restriction of hazardous substances (RoHS) and on the registration, evaluation, authorization and restriction of chemicals (REACH). In order to meet the requirements of its global customer base in the best possible way, the Group also complies with the respective provisions in many other regions of the world. Furthermore, ADVA Optical Networking contributes to industry-wide discussions focused on impacting future adjustments in relevant international legislation. Being involved in these discussions allows the Group to react early in an appropriate way.

Focus on product eco-friendliness, already in design phase

In addition, ADVA Optical Networking continually improves the eco-friendliness of its products, even when there are no related legally binding requirements to do so. The Group's design for low power process institutionalizes power consumption reviews as a part of the early design cycle. Lowest possible power consumption is as important a feature as the other features triggering the development of a product.

Use of returnable and reusable packaging material

The Group also contributes to the respectful utilization of natural resources by using returnable packaging material for the flow of goods between component vendors and the Group's facilities. ADVA Optical Networking aims to reuse the outer packaging from vendors for its own shipments. In order to do so, the Group in part customizes vendor packaging material to fit specific sales requirements.

Successful ISO 14001 repeat certification of all major facilities in 2013

ADVA Optical Networking's facilities in Germany, Poland, the U.S., the United Kingdom and China take advantage of state-of-the-art energy-saving building technology concepts. The Group has implemented a global environmental management system and underwent repeated ISO 14001 environmental management standard audits at all relevant facilities worldwide with all previous certifications confirmed (Meiningen, Berlin and Martinsried/Munich in Germany, Gdynia in Poland, Richardson (Texas) and Norcross (Georgia) in the U.S., York in the United Kingdom and Shenzhen in China) in 2013.

Carbon footprints for typical product configurations assessed

Finally, in 2013 ADVA Optical Networking has been performing various full life cycle assessments (carbon footprints) of typical configurations of both the Group's Ethernet access and WDM product lines. Introduced already in 2012, these assessments provide clear baselines against which to track progress.

Comprehensive Sustainability Reporting

Comprehensive GRI sustainability reporting

In order to make its sustainability work more transparent, ADVA Optical Networking has prepared Global Reporting Initiative (GRI) index data. [10] This index describes the Group's key sustainability activities and its main objectives related to employees, society and environment. Based on an internal review, ADVA Optical Networking determines this to be a C-level index for years 2011 to 2013 when graded against the GRI G3.1 guidelines. The GRI index for these years as well as additional corporate social responsibility information on ADVA Optical Networking can be found on the Group's website www.advaoptical.com (About Us / Corporate Social Responsibility).

Declaration on Corporate Governance and Corporate Governance Report

Compliance with the rules of proper corporate governance is of great importance to ADVA Optical Networking, it is the foundation for the Group's success. According to section 289a of the German Commercial Code (Handelsgesetzbuch, HGB), ADVA Optical Networking SE is obliged to publish a "declaration on corporate governance", and section 3.10 of the German Corporate Governance Code as amended on May 13, 2013 recommends that Management Board and Supervisory Board shall prepare a "corporate governance report". In order to facilitate public access to all respective data, ADVA Optical Networking integrates the "declaration on corporate governance" and the "corporate governance report" into one single publication on its website www.advaoptical.com (About Us / Investor Relations / Corporate Governance / Declaration on Corporate Governance and Corporate Governance Report).

[10] GRI was established in 1997 by the United Nations and the Coalition for Environmentally Responsible Economics (CERES). It organizes reporting on sustainability in a consistent manner and thereby makes it easier to compare objectives and performance.

Remuneration of Management and Supervisory Boards

The Management Board receives fixed compensation, a short and long-term variable bonus and stock options

The compensation of ADVA Optical Networking's Management Board members consists of fixed and variable components. In addition to a fixed salary, the members of the Management Board receive variable compensation in the form of bonus payments which are assessed based in part on short-term aspects and in part on long-term criteria focusing on the sustainable development of the Group. As additional long-term variable compensation, the Management Board members receive stock options within the scope of ADVA Optical Networking's stock option program.

In 2013, the combined fixed salary of the three members of the Management Board in office at year-end 2013 increased by 2.0% compared to 2012. The short-term variable compensation for both years is based on the Group's pro forma operating income (40%), the Group's revenues (20%), the Group's free cash flow (20%) as well as individual goals agreed with each member of the Management Board at the beginning of the respective year (20%). The short-term variable compensation is determined annually as compensation for the current year at the discretion of the Supervisory Board. Furthermore, as in 2012, a long-term variable compensation focusing on the sustainable development of the Group was defined in 2013 and will be paid to the members of the Management Board after three years, provided that minimum Group pro forma operating income margins, increasing year-by-year, are met for each of the three years. All members of the Management Board additionally receive a company car or a car allowance, as well as – in Germany – reimbursement of half of their social security contributions. Moreover, ADVA Optical Networking bears the costs of pecuniary damage liability insurance for the Management Board members, taking into account the statutory deductible amount. These benefits are partially taxable by the members of the Management Board as non-cash benefits. In addition, ADVA Optical Networking grants stock options to members of the Management Board. These option rights authorize the members of the Management Board to purchase a set number of shares in the Company once a fixed vesting period has elapsed.

At the end of Q1 2013, Christian Unterberger, Chief Sales & Marketing Officer, left the Company by mutual agreement. His areas of responsibility have been assumed by Chief Executive Officer Brian Protiva. In order to compensate for compliance with a noncompetition clause during the twelve months following Christian Unterberger's departure, a total amount of EUR 160 thousand has been agreed to be paid out to him in four instalments at the end of each quarter.

Total Management Board compensation payable for 2013 and 2012 was EUR 1,527 thousand and EUR 1,850 thousand, respectively. In 2013 and 2012, no loans or prepayments were granted to the members of the Management Board.

The Supervisory Board receives fixed compensation

As a result of the change of the remuneration system resolved by the Annual Shareholders' Meeting on June 4, 2013, the members of the Supervisory Board from July 23, 2012 (the date of the conversion of ADVA AG Optical Networking into an SE legal entity) do not currently receive any variable compensation. Thus, beyond the reimbursement of out-of pocket expenses, the compensation of the members of ADVA Optical Networking's Supervisory Board only consists of a fixed component paid out quarterly.

For the period from the beginning of 2012 until July 23, 2012, the Annual Shareholders' Meeting on June 4, 2013 approved variable compensation of EUR 25 thousand for the Supervisory Board of ADVA AG Optical Networking, the legal predecessor of ADVA Optical Networking SE. This variable compensation was paid out in 2013. With its conversion into ADVA Optical Networking SE on July 23, 2012, ADVA AG Optical Networking ceded to exist.

The total compensation payable to the members of the Supervisory Board of ADVA Optical Networking for 2013 amounted to EUR 235 thousand, after EUR 295 thousand for 2012.

Furthermore, ADVA Optical Networking bears the cost of pecuniary damage liability insurance for all members of the Supervisory Board. During 2013, no loans or advance payments were granted to members of the Supervisory Board.

Detailed information on the compensation structure of the individual members of the Management and Supervisory Boards can be found in note (34) to the consolidated financial statements.

Risk Report

ADVA Optical Networking's future development is subject to various risks, which in certain cases can also endanger the Group's continued existence. The Management Board has implemented a risk management and an internal control system that enables the Management Board to detect risks in due time, take corrective actions and benefit from opportunities. An essential aspect of the Group's strategy is its ability to anticipate developments in the marketplace and future customer needs. Special emphasis is given to product development and the quality of the Group's products. Due to ever-changing market trends and limited planning certainty as well as reliance on IT systems, data confidentiality and intellectual property, risks to ADVA Optical Networking's future cannot be completely excluded.

Risk Management System

Diversified business

Since ADVA Optical Networking was founded in 1994, its business has become more diversified. The Group's market is split into three global areas (enterprise networks, carrier infrastructure, Carrier Ethernet access), all with drivers largely independent of each other. ADVA Optical Networking markets its products and solutions in part via a variety of distribution partners and has become less dependent on these partners over the years. Beyond focusing on reducing revenue volatility, a comprehensive risk management system has been established, enabling the Group to detect risks in a timely manner and to take preventive and corrective actions accordingly. The risk management system is subject to scheduled reviews by the Group's internal audit function. The Management Board of ADVA Optical Networking SE recognizes that however good a risk management system may be, it cannot in all cases prevent the occurrence of events that may cause material damage to the Group.

Effective decision support and reporting system

ADVA Optical Networking is organized according to functional areas across all international locations. This is also reflected in the Management Board's split of responsibilities, in particular as related to risk management. The Management Board continuously analyzes the potential risks and implements the necessary measures to guard against them to the greatest extent possible. In recent years, ADVA Optical Networking has significantly improved its results-driven decision support and reporting system. The Group has established an appropriate risk management system across all departments with the purpose of quickly uncovering potential risks and taking corrective actions in a timely manner. These measures allow the Management Board to evaluate the present and future situation of the Group at all times. A combination of regular and ad-hoc reports present a thorough picture of current and future business developments.

Strategic goals are the basis of the risk management system

ADVA Optical Networking's strategic goals are the basis for this risk management system. These goals are profitable growth, Optical+Ethernet innovation, operational excellence and employee development. The strategic goals are reviewed by both the Management Board and the Supervisory Board on a yearly basis and amended where appropriate. They also constitute the basis for the Group's three-year business plan, which is reviewed and updated annually. Each of these goals is defined in detail and then broken down into specific departmental and individual targets. The strategic goals are traced to each individual employee, so that each employee can focus and be evaluated on his/her individual performance and contribution to ADVA Optical Networking's overall performance.

Revenues, pro forma operating income, net liquidity and Net Promoter Score operationalize strategic goals and represent ADVA Optical Networking's key performance indicators

ADVA Optical Networking measures the accomplishment of its strategic goals against revenues, pro forma operating income[1], net liquidity[2] and as a non-financial criterion customer satisfaction as measured by the Net Promoter Score[3]. These metrics represent the Group's key performance indicators. The Management Board sets target values for all four metrics for the year to come and measures actual values against the target values on a monthly basis for revenues and pro forma operating income, on a quarterly basis for net liquidity and on a yearly basis for the Net Promoter Score. In case of deviations from plan, corrective action can be taken quickly. This information is summarized and communicated to the Management Board in monthly, quarterly and yearly reports.

Monthly budget reviews, tight controls and processes

Moreover, budgets are reviewed on a monthly basis and adjusted if necessary. The Group's accounting, decision support and treasury departments provide monthly, globally consolidated reports on available cash funds and the development of margins and current assets (e.g., inventories and receivables). These reports also include budgeted/forecasted and actual revenues and expenditures. Structure and content of these reports must be adapted continuously to meet information requirements. ADVA Optical Networking has regularly updated credit limits in place for all customers. Material expenditures and investments must be approved in advance through an electronic purchase order system. In conjunction with continuously updated revenue and cash forecasts, a detailed monthly preview of anticipated Group developments within the next three to twelve months can be generated. In addition, ADVA Optical Networking's Management Board regularly analyzes the financial position and profitability of the Group, discusses all significant business transactions with the Supervisory Board and obtains its approval if necessary.

Comprehensive compliance system in place

In order to ensure observance of all applicable laws and regulations, ADVA Optical Networking has a code of conduct and a range of Group-wide policies in place which govern the Group's business operations and are mandatory for all employees to follow. The code is an extension of the Group's core values, and employees are encouraged to report suspected incidents of non-compliance and to seek support when having questions or suggestions. An external ombudsman (this role is currently covered by Frank Fischer, tax lawyer and former member of ADVA Optical Networking's Supervisory Board) and an externally operated ethics and compliance helpline enable confidential and anonymous reporting. Enforcement of compliance with all applicable laws and regulations and deriving internal policies is coordinated by ADVA Optical Networking's Chief Compliance Officer who reports to the Chief Executive Officer and the Supervisory Board.

The analytical tools and processes described above secure a constant and transparent reporting system across all divisions. In regular monthly reports and multiple webinars per year, the Management Board informs the extended worldwide management team about the current business development, business outlook, Group and departmental goals.

All major risks are described, as well as the internal controls, processes and tools that are used to mitigate these risks

In addition, ADVA Optical Networking systematically describes all major risks which may cause material harm to the Group or may even threaten its existence, as well as the internal controls, processes and tools that are used to mitigate these risks. A risk is classified as major if its severity and its probability of occurrence on a high-medium-low scale is each ranked "medium" at least. The list of major risks is subject to change, driven by input from within the organization and at least quarterly reviews by the Management Board. For each major risk identified, the Group assigns a dedicated risk owner who is responsible to report risk-related information periodically and to inform the Management Board immediately should the risk materialize. Compliance with this process is monitored by the Group's treasury department. Independent of specific risk ownership, all employees of ADVA Optical Networking are asked to escalate additional obvious risk items directly and informally to the Chief Financial Officer & Chief Operating Officer and the treasury department. At the end of 2013, ADVA Optical Networking had ranked 12 risks as major (end of 2012: 14), which are discussed in detail below.

12 risks ranked as major at the end of 2013

Competitive and Product Risks

Technology Leadership Risk

The market for Optical+Ethernet connectivity solutions is highly competitive and subject to rapid technological change. Competition in this market is characterized by various factors, such as price, functionality, service, scalability and the ability of systems to meet customers' immediate and future network requirements. Should ADVA Optical Networking be unable to adapt to changing market conditions, customer requirements or industry standards, the Group's development would be impacted negatively. The same is true if products cannot be seamlessly integrated into existing customer network infrastructures. This could lead to delays in installation, return of products or cancellation of orders, and would not only result in additional costs for warranty and repair services, but would also harm ADVA Optical Networking's overall reputation. Since most of the Group's competitors operate in a broader market and have considerably more resources available due to their greater size, ADVA Optical Networking must continue to leverage its competitive advantage in terms of functionality and efficiency of its solutions, as well as in terms of total cost for the customer. Preventive actions to achieve this include running advanced technology projects, keeping the Group's development roadmap up-to-date, testing product visions with customers, driving the evolution of intellectual property rights, monitoring and influencing standardization, minimizing dependency on legacy products, maximizing R&D efficiency and staying close to customers in order to identify differentiating technology opportunities.

Cost Leadership Risk

ADVA Optical Networking achieves cost leadership by its ability to scale economically. The loss of cost leadership would drastically reduce the Group's success in winning new business and would have a negative effect on gross and operating margins. The significant pricing pressure for Optical+Ethernet connectivity solutions must be met strategically by improving processes, controls and technology, while maintaining adequate R&D budgets. Preventive actions to achieve this include running focused cost reduction programs on existing products, identifying competitive price and cost targets for new products, monitoring product cost development throughout the development process and negotiating, tracking and forecasting product and related component costs.

Product Quality Risk

The deterioration of the quality of ADVA Optical Networking's products could lead to delays in installation, return of products or cancellation of orders, and could result in additional costs for warranty and repair services. In addition, the Group could face penalties and lawsuits, contract terminations and liability claims, which ultimately could lead to lower market shares and harm to ADVA Optical Networking's overall reputation. Preventive actions to avoid quality deterioration include continuously improving the Group's development processes, enhancing product testing, closely monitoring product return and customer complaint rates as well as analyzing respective root causes, optimizing complaint handling and supplier quality and measuring and analyzing customer satisfaction on a regular basis.

IT System Functionality and Availability Risk

There is significant risk that the Group temporarily or completely loses access to business-relevant data due to IT system failures or that access and processing speed falls below acceptable levels. This may have a negative impact on ADVA Optical Networking's business activities. The Group has put preventive measures in place in order to mitigate this risk. These measures include comprehensive network and application monitoring, access lines to major sites independent of general traffic, and application clustering.

Supplier Quality Risk

The quality of ADVA Optical Networking's products is heavily influenced by the quality of the components provided by suppliers and contract manufacturers. Component dysfunction may cause the Group's solutions not to work properly or in some cases not to work at all. This may lead to the disruption of customer deliveries, penalty payments, product recalls, delivery contract termination and loss of reputation. ADVA Optical Networking has put preventive measures in place to ensure appropriate supplier quality, including systematically qualifying components, monitoring supplier performance by means of business and financial reviews as well as audits, negotiating penalty clauses in supplier contracts, placing orders with second sources, building buffer stocks, having appropriate product liability insurance in place, and selectively replacing components in already installed systems with significant dysfunction potential.

Financial Risks

Inventory Risk

Technological obsolescence, as well as short-term changes in customer demand and manufacturing processes may trigger significant inventory depreciation. Preventive measures to minimize inventory depreciation include an integrated sales and operations planning process and monthly reviews of inventory depreciation requirements on item level involving the Finance and Operations functions. In 2013, inventory depreciation amounted to EUR 2.2 million after EUR 4.5 million in 2012.

Foreign Currency Risks

EUR/GBP and EUR/USD Volatility Impact on Cash Flows Risk

Due to a major portion of the Group's revenues and costs being generated in foreign currencies, ADVA Optical Networking is particularly subject to fluctuations in the EUR/USD and EUR/GBP exchange rates. In 2013, on a net basis, the Group saw significant GBP inflows and USD outflows, based on strong GBP operating cash flow generation and largely USD-denominated material purchasing, which was less than compensated by USD cash income. To combat fluctuations, the USD and GBP net cash flows in part are hedged against EUR using forward exchange agreements, based on the Group's forecasted EUR/USD and EUR/GBP exposure for the current year and the year to come, and taking into account ongoing fundamental analysis provided by a bank-independent foreign currency consultancy. Further information on the sensitivity of the Group's net income to fluctuations in foreign exchange rates is provided in note (27) to the consolidated financial statements. On December 31, 2013, ADVA Optical Networking had frame agreements in place with a total of 9 banks (December 31, 2012: 9 banks) to enter into respective hedging transactions. The importance of currency hedging, especially by means of derivative instruments and natural hedges through local purchasing and manufacturing will increase for ADVA Optical Networking in the future. Further expansion in non-EUR regions of the world is likely to raise the Group's foreign exchange cash flow exposure as well.

Foreign Currency-Related Price Risk

A weakening of foreign currencies, especially of the USD and the GBP, can have a significant financial impact on the ability to price ADVA Optical Networking's products competitively. Since many of the Group's major competitors are U.S. companies, they benefit from a weakening USD. This could result in a negative impact on the Group's level of competitiveness and business development and could endanger growth in markets outside the EUR zone. In order to mitigate this risk, ADVA Optical Networking tries to adjust non-EUR prices to fluctuations in foreign exchange rates and to include price adjustment clauses into its frame contracts with non-EUR customers.

Customer Payment Terms Risk

In ADVA Optical Networking's competitive Optical+Ethernet connectivity market, customers may ask to extend payment terms. The extension of the Group's weighted-average payment terms would have an adverse impact on working capital and cash levels. In order to mitigate this risk, there is a three-step process in place governing the escalation of payment terms extension requests. Also, at the end of 2013, the Group had frame contracts in place to sell receivables from two customers (at the end of 2012: from two customers) to financial institutions.

Customer On-Time Payment Risk

If customers pay their open invoices at a later point in time than contractually agreed, there is an adverse impact on working capital and cash levels. Also, once receivables become overdue, the likelihood of payment default increases. In 2013, depreciation on trade accounts receivable due to doubtful accounts amounted to EUR 0.6 million (2012: EUR 2.1 million). In order to mitigate the on-time payment risk, the root causes for a customer not paying in time are addressed in close collaboration between the Group's Finance and Sales organizations. Underlying product, service and billing issues are addressed, and in cases where there are no such issues or where such issues have been resolved successfully and open invoices are still not paid, customer credit limits are adjusted, customer shipments are stopped and/or customer prepayment will be required for future transactions.

Legal Risks

Intellectual Property Risk

ADVA Optical Networking currently relies on a combination of copyright and trademark laws, contractual rights, patents and trade secrecy laws to protect its intellectual property. Unauthorized parties may attempt to copy or otherwise obtain and use the Group's products or technology. Monitoring unauthorized use of products and technology is difficult, and the Group cannot be certain that steps taken will prevent unauthorized use of products and technology. If competitors are able to use the Group's products and technology, ADVA Optical Networking's ability to compete effectively could be harmed. Counter measures may prove insufficient in the future and result in conflicts regarding the usage of property rights and technologies. In particular, the continued expansion of the Group's presence in China carries the risk that less stringent regulations for intellectual property rights could lead to an infringement on ADVA Optical Networking's patents and other intellectual property. Such infringement of intellectual property rights could take the form of the production of illegal copies of the Group's products and solutions, and could cause considerable damage to the Group. Third parties may also assert that ADVA Optical Networking has violated their own intellectual property rights and copyright laws, and may claim license fees, indemnities or discontinuation of production and marketing of the relevant products. Related disputes could result in considerable cost to ADVA Optical Networking in its efforts to protect intellectual property, while also diverting considerable management resources. This could result in a negative impact on the Group's business activities. In order to mitigate the intellectual property risk, the Group uses a systematic approach to document inventions and to decide which of these inventions are filed with the relevant authorities in order to obtain intellectual property rights.

Capital Market Compliance Risk

Capital market compliance risk arises from violations of laws, rules and regulations, prescribed practices or ethical standards. This risk exposes ADVA Optical Networking to reputational damage, financial and non-financial sanctions. The Group's attention focuses on taking appropriate measures to prevent insider dealings, on reporting of directors' dealings, on ad-hoc news publishing, on voting rights reporting, on comprehensive quarterly financial reporting and on compliant preparation and execution of Shareholders' Meetings.

Major Risk Classification Changes During 2013

During 2013, two risks considered as major at the end of 2012 were re-classified as minor, the general macro-economic risk and the IT data security risk. The reclassifications were driven by reduced probability of occurrence.

Other Minor Risks

Additional minor risks

Beyond the 14 risks discussed above, there is a broad range of minor risks which can also have a negative impact on ADVA Optical Networking. These uncertainties include financial risks such as the inability to secure financing, impairment of intangible assets and changes in interest rate levels, time risks related to carrier investment cycles and to distribution partnerships, legal risks pertaining to potential claims under product and warranty liabilities, risk from unauthorized access to confidential data, customer concentration risk and risks related to acquisitions. However, the Management Board of ADVA Optical Networking does not consider any of these or other uncertainties to be likely or to have a major impact on the Group.

Opportunity Identification

The identification of opportunities results from applying the same analytical tools and processes as described in the "risk management system" section above. Current opportunities are discussed in the "outlook" section further below.

Overall opportunity and risk balance net at about the same level than a year ago, no current risks are endangering the Group's survival

Overall Opportunity and Risk Assessment

Based on careful inspection of the Group's opportunity and risk profile at the time of the preparation of the Group management report, the Management Board of ADVA Optical Networking believes that the Group's opportunities in the Optical+Ethernet connectivity market clearly outweigh the risks identified. The Management Board has not identified any risks that pose a danger to ADVA Optical Networking's survival, and to the Management Board there are no risks evident that may endanger the future existence of the Group. ADVA Optical Networking's overall opportunity and risk balance net is at about the same level than at the time the Group management report of the prior year had been prepared. The global macro environment is less uncertain, there are additional market opportunities driven by LTE-Advanced rollouts and increased enterprise cloud service adaption, and IT data security at ADVA Optical Networking has improved. Also, the ongoing ramp of the Group's development activities has further strengthened its technology positioning and product quality, reducing ADVA Optical Networking's competitive and product risks. On the other hand, the volatile revenue development in 2013 related to significant customer concentration and volatile business with a major distribution partner led to lower operating margins than in the prior year and increased uncertainty about the short-term prospects of ADVA Optical Networking.

Internal controls related to financial reporting designed around COSO framework

Internal Controls Related to Financial Reporting

The Management Board of ADVA Optical Networking is responsible for establishing and maintaining an adequate system of internal controls. It has implemented an internal control system that enables the Management Board to ensure completeness, accuracy and reliability of financial reporting at Group and legal entity level. When designing its internal control system, ADVA Optical Networking used the COSO framework[11] as a key reference and source of guidance. The internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting. No system of internal control over financial reporting, including one determined to be effective, may prevent or detect all misstatements.

Control environment backed by the Management Board's leadership principles

Control Environment

The control environment is the foundation of the internal control system in every organization. ADVA Optical Networking fosters an environment of openness and integrity with a clear commitment to excellence, competence and the development of its employees. The Group's leadership principles of integrity/honesty, decisiveness and respect are based on this philosophy, and the culture is reflected in the overall tone set by the Management Board. ADVA Optical Networking has a clear organizational structure with well-defined authorities and responsibilities. The bodies charged with the governance and control of the Group (Management Board, Supervisory Board) actively participate in the running and steering of the business. The business is managed on a global basis and run via functional areas. Financial steering of the Group and financial stewardship for individual legal entities is handled by the Chief Financial Officer & Chief Operating Officer, under the Audit Committee's control.

[11] Five major accounting organizations formed a group known as COSO (Committee of Sponsoring Organizations of the Treadway Commission), to provide guidance on evaluating internal control. They issued this guidance as the COSO Internal Control Framework.

Risk Assessment

As part of the internal controls related to financial reporting, the risk assessment follows the process described in the "risk management system" section.

Information technology controls suited to complexity of business units

Control Activities

At an individual entity level. ADVA Optical Networking's larger and more complex business units use an integrated enterprise resource planning solution, which also serves as general ledger system. Information technology controls have been implemented to restrict user access, ensure proper authorization of changes to the system and efficient handling of user help desk requests. Specific processes are defined and applied for the following reporting cycles in those business units: cash reporting, revenue recognition, accounts payable, capitalization of development expenses and subsidies, inventory reporting, fixed assets, payroll and provisions. ADVA Optical Networking carries out monthly analytical reviews and quarterly balance sheet reviews based on a four-eyes principle between the local accounting and the consolidation functions.

For the consolidated financial statements, those balance sheet and income statement positions requiring a significant degree of judgment and estimation when being valued are determined and analyzed with the involvement of management. This is the case for impairment testing reviews (annual or when a triggering event occurs), capitalization of development projects (when the industrialization stage is reached) and tax reporting and review, specifically deferred taxes (quarterly). ADVA Optical Networking additionally carries out monthly intercompany reconciliations as part of the consolidation process and analytical reviews of actual vs. expected results based on a four-eyes principle between the financial planning and the consolidation functions.

Global accounting policies, reporting guidelines and closing calendar

All business units follow a set of global accounting policies and reporting guidelines. The financial statements preparation process is monitored globally via a calendar that is communicated to all involved parties on a monthly basis. Checklists are completed both in the individual business units and at the consolidation level to ensure completeness of all closing steps. Periodic reviews by Group management are conducted to detect errors and omissions.

Effective information and communication with the Management Board

Information and Communication Tools

The internal control system at ADVA Optical Networking is supported by tools to store and exchange information, enabling the Management Board to make informed business decisions about financial reports and disclosures. The following components ensure proper information and communication for financial reporting:

- Accounting systems for individual entities are matched to the degree of complexity of the business unit. For most entities, an integrated enterprise resource planning system which also serves as general ledger system is in place. All local accounts are mapped to the Group chart of accounts, which is used Group-wide.

- The Group consolidation is supported by a database tool which is linked to the enterprise resource planning and financial planning systems via interfaces. The global financial planning system is used extensively in analyzing actual vs. expected results and thus monitoring the results of the consolidation.

- There are global accounting policies for the more complex financial statement positions of the Group and a Group chart of accounts for all other financial guidance. Accounting policies are updated regularly and are implemented only after a thorough internal review and training.

Transparent reporting and follow-up on control deficiencies

Internal Monitoring
As part of the ongoing monitoring, the Chief Financial Officer & Chief Operating Officer is informed of all material misstatements and control breakdowns at Group and business unit level on a quarterly basis in the executive summary to the financial statements. The reporting of deficiencies follows the principles of open and transparent communication, and follow-up is ensured through regular calls where corrective actions are presented.

Internal audit function for financial processes

Internal Financial Audit
In order to monitor significant activities, to identify and minimize risks, to improve efficiency of financial processes and to support decision-making, ADVA Optical Networking maintains an internal audit function to review financial processes. Financial processes are globally harmonized in so far as a global process does not contravene local regulations. The internal audit review encompasses global financial processes as well as business-unit specific processes where necessary to satisfy local requirements.

Based on an annual risk assessment for key financial processes, the internal audit function proposes an audit program for the year which is discussed with and ratified by the Chief Financial Officer & Chief Operating Officer and the Audit Committee. The internal audit function performs appropriate internal audit procedures throughout the year, and presents the standardized internal audit reports to the Audit Committee.

Actions to adjust processes or enhance internal controls are initiated based on the recommendations included in the internal audit reports. The internal audit function regularly tracks actual implementation of these recommendations.

Events After the Balance Sheet Date

There were no events after the balance sheet date that impacted the financial position of the Group on December 31, 2013 or its financial performance for the year then ended, nor were there any events considered material for disclosure.

Outlook

Average addressable market growth of 12% per year expected through 2016

Based on the macro-economic environment described above, ADVA Optical Networking expects its total market to grow by an average 12% per year between 2013 and 2016.[6] Enterprise networks are expected to show the strongest growth within this segment.

Growth driven by increasing bandwidth demand and ongoing replacement of incumbent protocols with Ethernet

The growth of the overall market is primarily driven by steadily increasing bandwidth demand for wireless and wireline communication from residential end users and enterprises, with carriers continuously investing in new networking infrastructure solutions. Carrier decisions to substantially increase coverage and access capabilities of residential triple play services (data, voice and video) as well as the accelerated move to 4G wireless technology were major drivers for many next-generation network infrastructure builds. Data storage, cloud applications, the convergence of enterprise networks and virtualization of storage and compute applications across multiple data centers have been the main drivers for enterprise connectivity. Furthermore, the Ethernet protocol has now evolved to be the standard carrier network protocol, replacing legacy protocols such as SONET/SDH, ATM and Frame Relay.

Additional details on the projected market environment until 2016 as well as the resulting opportunities are discussed in the "general economic and market conditions" section further above.

Strategic goals

Based on the trends mentioned above, as in the prior year, ADVA Optical Networking will concentrate on the following four strategic elements:

- Grow global revenues profitably through continued strong direct sales and marketing efforts with a solid focus on key accounts, new customer wins, optimized distribution partnerships and non-hardware business.

- Expand the Group's proven innovation leadership by meeting strategic customers' demand for advanced networking solutions quickly and comprehensively.

- Maintain operational excellence by further focusing on industry-leading processes and best-in-class execution, which will result in quality leadership, improved efficiency and increased overall customer satisfaction.

- Recruit, retain, motivate, educate and nurture the Group's employees to achieve high levels of performance, personal growth and job satisfaction, while keeping attrition rates low.

2013 expectations have been met in part only

Looking back at 2013, ADVA Optical Networking made partial progress in meeting these strategic elements:

2013 revenues were down 5.9% compared to 2012, below overall market growth[6] and below the expectations of the Management Board of growing revenues as announced in the 2012 Group management report. While the Group was able to further increase its overall customer base in 2013 and expand into new industry verticals, volatile business with select major customers led to uneven quarterly revenue development in 2013. This resulted in a significant decline of the Group's pro forma operating income[1], which was at EUR 8.6 million in 2013 after EUR 21.8 million in 2012. Operating income at EUR 7.0 million in 2013 declined as well, after EUR 18.8 million in 2012, and fell behind the expectations of the Management Board of growing operating income as announced in the 2012 Group management report.

As for innovation leadership, ADVA Optical Networking was able to expand its position in 2013. The Group has continued to bring new features and capabilities to the market and to differentiate itself with technology. New releases for the mobile backhaul segment included adding capabilities to its 10G demarcation solutions as well as caching solutions for the mobile networks. ADVA Optical Networking also developed the mini-grandmaster clock functionality, the latest in a series of updates to the FSP 150 Syncjack™ timing distribution and assurance technology developed to simplify the migration to LTE-Advanced radio access networks, thereby helping carriers upgrade existing service edge routers and switches. For data center connectivity, the Group's ultra-compact 16Gbit/s Fibre Channel card, the first of its kind to achieve Brocade qualification, expands the capabilities of the FSP 3000 platform and is a key component for enterprises seeking to evolve their high-density server virtualization, cloud architectures and storage applications. In September 2013, as an industry-first SDN solution, ADVA Optical Networking successfully demonstrated a virtualized optical transmission network using OpenFlow-based control, developed in partnership with IBM and Marist College. With its innovative connectivity solutions portfolio including state-of-the art Ethernet access synchronization and assurance features as well as its 100G encryption technology for both metro and regional networks, the Group is well positioned to benefit from these technology trends.

Furthermore, ADVA Optical Networking maintained operational excellence in 2013. In a volatile business environment, the Group remained disciplined in controlling its operational costs, thereby enabling it to quickly adapt to changing circumstances whilst maintaining a strong focus on profitability. With strict controls in place and tight working capital management, ADVA Optical Networking maintained a strong cash position throughout the year. At year-end 2013, net liquidity at EUR 41.7 million reached a quarter-end record high. This development was in line with the expectations of the Management Board of growing net liquidity as announced in the 2012 Group management report. In addition, with its market-leading efficiency and delivery performance, ADVA Optical Networking won the prestigious annual supply chain management award in 2013, presented annually in Germany to the company with the most effective value chain in the manufacturing industry. The awarding bodies believed ADVA Optical Networking's global end-to-end and cross-enterprise segmentation is unique and provides the Group with a clear competitive edge. As for customer satisfaction, ADVA Optical Networking uses the Net Promoter Score[3] metric to track progress. For 2013, the score was at a strong +21%, but still below the +29% achieved in 2012.

On the employee side, ADVA Optical Networking added select additional talent in 2013, mostly in its research & development organization via the acquisition of Biran High-Tech Advisors Ltd (renamed to ADVA Optical Networking Israel Ltd.). Based on competitive compensation programs and a rewarding work environment with comprehensive education opportunities, the Group maintained the high motivation of its employees in 2013, as reflected in the strong results of the employee satisfaction survey conducted during the year.

Return to growth and improvement of ADVA Optical Networking's profitability targeted

ADVA Optical Networking targets to return to growth in 2014 and to improve the profitability of the Group. This is based on the strategic focus described above, a unique combination of factors differentiating ADVA Optical Networking from its peers and the ongoing growth expected in the telecommunications industry:

Good environment for further market growth

- Major investments by carriers around the world are inevitable. While growth in the Americas and the Asia-Pacific region was stronger than in the EMEA region in 2013, EMEA is poised to catch up, as reflected in current carrier projects such as Deutsche Telekom's EUR 30 billion and Vodafone's GBP 7 billion investment plans. Moreover, massive LTE rollouts in Brazil, China and Russia will fuel the market as well. In addition, enterprise cloud service adoption is accelerating. Investment in data centers and their requisite technologies will remain robust in the near term, and enterprises are investing to improve application performance, increase security, and reduce costs.

Unique combination of factors differentiates ADVA Optical Networking from its peers

- These exciting opportunities in ADVA Optical Networking's industry will support its strategic focus to be the trusted partner for innovative connectivity solutions. The combination of cost-effective innovation, short development and delivery times, a broad and growing customer base and well-balanced distribution model differentiates ADVA Optical Networking from its peers and will further fuel its sustainable business model.

In 2014, revenues, pro forma operating income and net liquidity are expected to grow moderately, and customer satisfaction is forecasted to increase significantly

Based on these factors, the Management Board of ADVA Optical Networking expects 2014 revenues to grow moderately. Under this assumption, the Management Board of ADVA Optical Networking also expects its 2014 pro forma operating income and net liquidity to increase slightly. The Group will invest selectively in its product engineering, selling & marketing and general & administrative functions. Further, with ongoing focus on innovation, quality and service, the Management Board of ADVA Optical Networking forecasts customer satisfaction as measured by the Net Promoter Score[3] to improve significantly in 2014. Actual results may differ materially from expectations, provided that risks materialize or the underlying assumptions prove unrealistic. The major risks facing ADVA Optical Networking are discussed in the "risk report" section further above.

Meiningen, February 17, 2014

Brian Protiva

Christoph Glingener

Jaswir Singh

IFRS Consolidated Financial Statements

What is the Foundation of Trust?

For the Stock Exchange of Thailand trust is the cornerstone of their business. It is something they pride themselves on. It is what customers expect from them. An always-on and dependable network is a key part of this trust. Data is critical to their success and the success of their customers. We understand these demands. That's why we have been working with them for many years. Our FSP 3000 connects their data centers. With our connectivity solution in place they know their data is safe, secure and readily available.

Consolidated Statement of Financial Position

(in thousands of EUR)

Assets	Note	Dec. 31, 2013	Dec. 31, 2012
Current assets			
Cash and cash equivalents	(7)	80,934	70,625
Trade accounts receivable	(8)	52,739	55,464
Inventories	(9)	40,074	41,339
Tax assets	(22)	379	136
Other current assets	(10)	4,651	6,734
Total current assets		**178,777**	**174,298**
Non-current assets			
Finance leases	(11)	16	51
Property, plant and equipment	(11)	21,866	23,287
Goodwill	(11)	19,875	19,876
Capitalized development projects	(11)	52,080	47,497
Purchased technology	(11)	1,012	1,185
Other intangible assets	(11)	1,687	2,401
Investments in associates and joint ventures	(6)	782	783
Loans to associates and joint ventures	(6)	229	-
Deferred tax assets	(22)	14,997	12,491
Other non-current assets	(10)	1,757	2,226
Total non-current assets		**114,301**	**109,797**
Total assets		**293,078**	**284,095**

Equity and liabilities	Note	Dec. 31, 2013	Dec. 31, 2012
Current liabilities			
Finance lease obligations	(12)	5	27
Financial liabilities	(13)	4,199	14,729
Trade accounts payable	(14)	26,515	38,078
Advance payments received		335	757
Provisions	(15)	8,245	5,293
Tax liabilities	(22)	2,029	4,935
Deferred revenues	(16)	9,972	8,607
Other current liabilities	(14)	20,572	19,258
Total current liabilities		**71,872**	**91,684**
Non-current liabilities			
Finance lease obligations	(12)	9	14
Financial liabilities	(13)	34,997	14,255
Provisions	(15)	1,407	739
Deferred tax liabilities	(22)	18,304	14,169
Deferred revenues	(16)	6,513	6,370
Other non-current liabilities	(14)	2,156	2,955
Total non-current liabilities		**63,386**	**38,502**
Total liabilities		**135,258**	**130,186**
Stockholders' equity	(17)		
Share capital		48,023	47,823
Capital reserve		307,131	306,763
Accumulated deficit		-195,360	-212,082
Net income		5,507	16,722
Accumulated other comprehensive loss		-7,481	-5,317
Total stockholders' equity		**157,820**	**153,909**
Total equity and liabilities		**293,078**	**284,095**

Consolidated Income Statement

(in thousands of EUR, except earnings per share and number of shares)	Note	2013	2012
Revenues	(18)	**310,702**	**330,069**
Cost of goods sold		-189,292	-198,464
Gross profit		**121,410**	**131,605**
Selling and marketing expenses		-47,114	-46,803
General and administrative expenses		-26,349	-25,985
Research and development expenses		-43,503	-42,042
Other operating income	(19)	3,120	2,286
Other operating expenses	(19)	-589	-227
Operating income		**6,975**	**18,834**
Interest income	(20)	134	158
Interest expenses	(20)	-1,278	-1,321
Other financial gains and losses, net	(21)	-1,475	834
Income before tax		**4,356**	**18,505**
Income tax (expense) benefit, net	(22)	1,151	-1,783
Net income		**5,507**	**16,722**
Earnings per share in EUR	(24)		
basic		0.11	0.35
diluted		0.11	0.34
Weighted average number of shares for calculation of earnings per share			
basic		47,897,901	47,626,641
diluted		48,586,198	48,782,175

Consolidated Statement of Comprehensive Income

(in thousands of EUR)	Note	2013	2012
Net income		**5,507**	**16,722**
Exchange differences on translation of foreign operations		-2,164	-481
Total comprehensive income	(17)	**3,343**	**16,241**

In 2013 and 2012, no items were reclassified (recycled) from comprehensive income to profit or loss. Moreover, there will be no reclassifications to profit or loss from the existing positions included in the consolidated statement of comprehensive income in future periods.

Consolidated Cash Flow Statement

(in thousands of EUR)	Note	2013	2012
Cash flow from operating activities			
Income before tax		4,356	18,505
Adjustments to reconcile income before tax to net cash provided by operating activities			
Non-cash adjustments			
Amortization of non-current assets	(11)	27,938	26,282
Loss from disposal of property, plant and equipment and intangible assets	(11)	243	117
Stock compensation expenses	(31)	913	1,344
Other non-cash expenses		52	22
Foreign currency exchange differences		-1,251	-1,390
Changes in assets and liabilities			
Decrease (increase) in trade accounts receivable		2,725	-590
Decrease (increase) in inventories		1,265	-4,803
Decrease (increase) in other assets		2,538	2,406
Increase (decrease) in trade accounts payable		-11,563	4,854
Increase (decrease) in provisions		3,406	-413
Increase (decrease) in other liabilities		1,358	-176
Income tax paid		-567	-1,002
Net cash provided by operating activities		**31,413**	**45,156**

Details on the preparation of the consolidated cash flow statement are included in note (23).

	Note	2013	2012
Cash flow from investing activities			
Proceeds from disposal of property, plant and equipment and intangible assets		115	37
Proceeds from government grants	(11)	414	-
Investments in property, plant and equipment	(11)	-7,409	-9,192
Investments in intangible assets	(11)	-23,188	-25,012
Acquisition of investments in associates	(6)	-	-782
Payments for loans to associates	(6)	-229	-
Net cash received from acquisition of affiliated companies	(6)	294	-
Interest received		72	156
Net cash used in investing activities		**-29,931**	**-34,793**
Cash flow from financing activities			
Proceeds from capital increase and exercise of stock options	(17)	375	634
Cash repayment of option bonds and other share-based compensation instruments	(31)	-299	-214
Payments for finance leases		-17	-27
Increase in financial liabilities	(13)	24,900	11,368
Cash repayment of financial liabilities	(13)	-14,729	-10,312
Interest paid		-1,189	-1,504
Net cash provided by / (used in) financing activities		**9,041**	**-55**
Net effect of foreign currency translation on cash and cash equivalents		-214	1,207
Net change in cash and cash equivalents		**10,309**	**11,515**
Cash and cash equivalents on January 1		70,625	59,110
Cash and cash equivalents on December 31		**80,934**	**70,625**

Consolidated Statement of Changes in Stockholders' Equity

(in thousands of EUR, except number of shares)	Share capital: Number of shares	Share capital: Par value	Capital reserve	Net income and accumulated deficit	Accumulated other comprehensive loss	Total
Balance on January 1, 2012	**47,524,875**	**47,525**	**305,379**	**-212,082**	**-4,836**	**135,986**
Capital increase, including exercise of stock options and option bonds	297,777	298	336			634
Stock options outstanding and option bonds outstanding		1,048				1,048
Net income				16,722		16,722
Exchange differences on translation of foreign operations					-481	-481
Total comprehensive income				16,722	-481	16,241
Balance on December 31, 2012	**47,822,652**	**47,823**	**306,763**	**-195,360**	**-5,317**	**153,909**
Capital increase, including exercise of stock options	200,175	200	175			375
Stock options outstanding			790			790
Reclassification to non-current provisions			-597			-597
Net income				5,507		5,507
Exchange differences on translation of foreign operations					-2,164	-2,164
Total comprehensive income				5,507	-2,164	3,343
Balance on December 31, 2013	**48,022,827**	**48,023**	**307,131**	**-189,853**	**-7,481**	**157,820**

Details on changes in stockholders' equity are presented in note (17).

Notes to the Consolidated Financial Statements

Summary of Accounting Policies

(1) Information About the Company and the Group

The consolidated financial statements of ADVA Optical Networking SE, Märzenquelle 1–3, 98617 Meiningen, Germany, (hereinafter referred to as "the Company") for the year ended December 31, 2013, were authorized for issue in accordance with a resolution of the Management Board on February 17, 2014.

The ADVA Optical Networking Group (hereinafter referred to as "ADVA Optical Networking" or "the Group") develops, manufactures and sells optical and Ethernet-based networking solutions to telecommunications carriers and enterprises to deliver data, storage, voice and video services.

Telecommunications service providers, private companies, universities and government agencies worldwide use the Group's systems. ADVA Optical Networking sells its product portfolio both directly and through an international network of distribution partners.

(2) Basic Principles for the Preparation of the Consolidated Annual Financial Statements

The Group's consolidated annual financial statements for the financial years ended December 31, 2013, and December 31, 2012, are prepared in accordance with the International Financial Reporting Standards (IFRS) published by the International Accounting Standards Board (IASB), as applicable in the European Union (EU). The consolidated financial statements have been prepared under the historical cost convention, as modified by the valuation of certain derivative financial instruments and share-based compensation transactions at fair value through profit and loss.

The consolidated annual financial statements are presented in EUR. Unless otherwise stated, all amounts quoted are in thousands of EUR. The balance sheet is separated into current and non-current assets and liabilities. The classification of income and expenses in the income statement is based on their function within the entity. When items on the balance sheet and in the income statement are summarized in the interest of clarity, this is explained in the notes to the consolidated financial statements. The additional disclosure requirements in order to comply with section 315a paragraph 1 of the German Commercial Code (Handelsgesetzbuch, HGB) have all been met.

The annual financial statements of the individual subsidiaries of the holding company ADVA Optical Networking SE, as subsumed in the consolidated annual financial statements, are all prepared using the same accounting and valuation policies and the same balance sheet date.

(3) Effects of New Standards and Interpretations

The accounting policies followed are consistent with those of the prior financial year, except for the adoption of new and amended IFRSs and interpretations (IFRICs) during the year.

Standards, amendments and interpretations applicable for the first time in 2013

The Group has adopted the following new or revised IFRSs and IFRIC interpretations in 2013. The application has not had a material impact on the amounts reported for the current and prior years but may affect the accounting for future transactions or arrangements.

Standard	Topic	First-time adoption*	Impact on the financial position and performance
IAS 1	Presentation of Financial Statements – Presentation of Items of Other Comprehensive Income (amendments to IAS 1)	Jul. 1, 2012	none
IAS 19	Employee Benefits (amendments)	Jul. 1, 2013	none
IFRS 1	First-time Adoption of International Financial Reporting Standards: Government Loans (amendments to IFRS 1)	Jan. 1, 2013	none
IFRS 7	Financial Instruments – Disclosures: Offsetting Financial Assets and Financial Liabilities (amendment)	Jan. 1, 2013	none
IFRS 13	Fair Value Measurement (new standard)	Jan. 1, 2013	none
Annual improvements 2011	The improvements include changes to: • IFRS 1 – First-time Adoption • IAS 1 – Financial Statement Presentation • IAS 16 – Property Plant and Equipment • IAS 32 – Financial Instruments: Presentation • IAS 34 – Interim Financial Reporting	Jan. 1, 2013	none

* To be applied in the first reporting period of a financial year beginning on or after this date.

The main change resulting from the amendments to IAS 1 is a requirement for entities to group items presented in "other comprehensive income" (OCI) based on whether they are potentially reclassifiable to profit or loss subsequently. The amendments do not address which items are presented in OCI. The adoption did not result in any effect on the financial reporting.

The amendment to IFRS 7 includes new disclosures to facilitate comparison between those entities that prepare IFRS financial statements to those that prepare financial statements in accordance with US GAAP. This mainly relates to disclosures of gross and net amounts resulting from offsetting as well as amounts for existing offsetting rights, which do not meet the accounting offsetting criteria.

IFRS 13 aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements. The requirements do not extend the use of fair value accounting.

New accounting pronouncements endorsed by the EU requiring application in future periods

Standard	Topic	First-time adoption*	Expected impact on the financial position and performance
IAS 27	Separate Financial Statements (revised 2011)	Jan. 1, 2014	none
IAS 28	Investments in Associates and Joint Ventures (revised 2011)	Jan. 1, 2014	none
IAS 32	Financial Instruments – Presentation: Offsetting Financial Assets and Financial Liabilities (amendment)	Jan. 1, 2014	none
IAS 36	Disclosure of Information about the Recoverable Amount of Impaired Assets (amendment)	Jan. 1, 2014	none
IAS 39	Novation of Derivatives (amendment)	Jan. 1, 2014	none
IFRS 10	Consolidated Financial Statements (new standard)	Jan. 1, 2014	none
IFRS 11	Joint Arrangements (new standard)	Jan. 1, 2014	none
IFRS 12	Disclosure of Interests in Other Entities (new standard)	Jan. 1, 2014	none
Amendments to IFRSs 10, 11 and 12 on transition guidance	Additional transition relief to IFRSs 10, 11 and 12 and guidance on disclosures related to unconsolidated structured entities	Jan. 1, 2014	none

* To be applied in the first reporting period of a financial year beginning on or after this date.

IAS 27 (revised 2011) includes the remaining provisions on separate financial statements after the control provisions of IAS 27 have been included in the new IFRS 10.

IAS 28 (revised 2011) includes the requirements for joint ventures, as well as associates, to be equity accounted following the issue of IFRS 11.

IFRS 10 replaces requirements formerly included in IAS 27 and SIC 12. The objective of IFRS 10 is to establish a uniform control concept as well as principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities. It defines the principle of control and sets out accounting requirements for the preparation of consolidated financial statements.

IFRS 11 replaces regulations of IAS 31 and SIC 13 and is a more realistic reflection of joint arrangement by focusing on the rights and obligations of the arrangement rather than its legal form.

IFRS 12 includes disclosure requirements for affiliated companies, joint arrangements, associates as well as special purpose vehicles.

The Group does not plan to adopt early neither new standards nor amendments.

New accounting requirements not yet endorsed by the EU

The IASB and the IFRIC have issued further Standards and Interpretations in 2013 and previous years. The application is not yet mandatory for the financial year 2013 and in addition is subject to the adoption by the EU.

Standard	Topic	First-time adoption*	Expected impact on the financial position and performance
IAS 19	Employee Benefits (amendments)	Jul. 1, 2014	none
IFRS 9	Financial Instruments (new standard)	not defined**	under review
IFRS 14	Regulatory Deferral Accounts (new standard)	Jan. 1, 2016	none
Annual improvements 2013	The improvements include changes to: • IFRS 2 – Share-based Payment • IFRS 3 – Business Combinations • IFRS 8 – Operating Segments • IFRS 13 – Fair Value Measurement • IAS 16 – Property, Plant and Equipment • IAS 38 – Intangible Assets • IAS 24 – Related Party Disclosures	Jul. 1, 2014	under review
Annual improvements 2013	The improvements include changes to: • IFRS 1 – First-time Adoption • IFRS 3 – Business Combinations • IFRS 13 – Fair Value Measurement • IAS 40 – Investment Property	Jan. 1, 2015	under review
IFRIC 21	Levies	Jan. 1, 2014	under review

* To be applied in the first reporting period of a financial year beginning on or after this date.

** The IASB decided at the July 2013 Board meeting to defer the mandatory effective date and rather leave it open pending the finalization of the impairment, classification and measurement requirements.

IFRS 9 is the first standard issued as part of a wider project to replace IAS 39. IFRS 9 retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets: amortized cost and fair value. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. The guidance in IAS 39 on impairment of financial assets and hedge accounting continues to apply. The impact on the financial reporting has not yet been determined.

IFRIC 21 includes guidelines for the recognition of liabilities related to levies imposed by administrative bodies. The interpretation applies for levies that are accounted for according to IAS 37 as well as governmental charges with distinct payment date and amount.

Besides the described standards, the adoption of new or revised standards and interpretations – from today's perspective – will not have a material impact on the financial position and performance of the Company or the Group. The Group does not plan an early adoption of these standards.

(4) Significant Accounting Policies

Principles of consolidation

All companies in which ADVA Optical Networking SE has direct or indirect control through subsidiaries are fully consolidated on the date of change of control to ADVA Optical Networking SE. Companies are deconsolidated on the date when ADVA Optical Networking SE's control ceases.

Intercompany revenues, expenses, income, receivables and payables within the Group are netted.

Intercompany profits that arise from deliveries of products and services provided within the Group are eliminated.

Business combinations

Business combinations from January 1, 2010 are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. For each business combination, the acquirer measures the non-controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition costs incurred are expensed.

When a Group company acquires a business, it assesses the financial assets and liabilities acquired for appropriate classification and designation in accordance with the contractual terms, economic circumstances and relevant conditions on the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is re-measured to fair value on the acquisition date through profit and loss.

Any contingent consideration to be transferred by the acquirer will be recognized at fair value on the acquisition date. Subsequent changes to the fair value of the contingent consideration that is deemed an asset or liability will be recognized in accordance with IAS 39 either in profit or loss or as a change to other comprehensive income. If the contingent consideration is classified as equity, it shall not be re-measured until it is finally settled within equity.

Goodwill is initially measured at cost being the excess of the consideration transferred over the Group's net identifiable assets acquired and liabilities assumed. If this consideration is lower than the fair value of the net assets of the company acquired, the difference is recognized in profit or loss after reassessment.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

Where goodwill forms part of a cash-generating unit and where part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

Investments in associates and in joint ventures
The equity method according to IAS 28 (Investments in Associates) is used to account for investments in entities in which ADVA Optical Networking SE holds 20% to 50% of the voting rights, either directly or indirectly, and over whose operating and financial policy decisions ADVA Optical Networking SE exercises significant influence (associated companies). The investment is initially recognized at cost, and the carrying amount is increased or decreased to recognize the investor´s share of the profit or loss generated. The Group share of the profit or loss of investments accounted for by the equity method is recognized in the consolidated income statement, whereas the share of changes in the equity of investments accounted for by the equity method that has not been recognized in profit or loss is shown in the reserves of the consolidated equity. In case the Group share of losses exceeds the carrying amount of the investment accounted for by the equity method, no further losses are recognized at Group level. Goodwill relating to an investment accounted for by the equity method is included in the carrying amount of the investment. Upon loss of significant influence over an associate, the Group measures and recognizes any retaining investment at its fair value. Upon loss of significant influence, any difference between the carrying amount of the associate and the fair value of the retaining investment and proceeds from disposal are recognized in profit or loss.

The equity method is equally used for entities in which ADVA Optical Networking exercises joint control (joint ventures). These are jointly controlled entities, whereby the venturers have a contractual arrangement that establishes joint control over the economic activities of the entity.

Foreign currency translation
TThe functional currency of each Group company is the currency of the main economic environment in which the company operates. The reporting currency of ADVA Optical Networking's consolidated financial statements is the functional currency of the parent company, ADVA Optical Networking SE (EUR).

Transactions in foreign currencies are initially recorded by the Group entities at their respective functional currency rates prevailing on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency spot rate of exchange ruling on the reporting date. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates on the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates on the date when the fair value is determined.

The assets and liabilities of foreign operations are translated into EUR at the rate of exchange prevailing on the reporting date, and their income statements are translated at the average rate for the reporting period. The exchange differences arising from the translation are recognized in accumulated other comprehensive income. On disposal of a foreign operation, the component of accumulated other comprehensive income relating to that particular foreign operation is recognized in the income statement.

Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amount of assets and liabilities arising on acquisition are treated as assets and liabilities of the foreign operation and translated at the closing rate.

The relevant currency translation rates are listed below:

	Closing rate on Dec. 31, 2013	Average rate for the period Jan. 1 to Dec. 31, 2013	Closing rate on Dec. 31, 2012	Average rate for the period Jan. 1 to Dec. 31, 2012
USD/EUR	1.3783	1.3276	1.3219	1.2852
GBP/EUR	0.8364	0.8487	0.8183	0.8112
NOK/EUR	8.4255	7.8057	7.3855	7.4794
JPY/EUR	145.0200	129.4922	113.6364	102.0408
CNY/EUR	8.3555	8.1630	8.3472	8.1235
SGD/EUR	1.7481	1.6607	1.6179	1.6062
SEK/EUR	8.9283	8.6492	8.6133	8.7032
PLN/EUR	4.1487	4.1962	4.0783	4.1859
HKD/EUR	10.6886	10.2948	10.2564	9.9800
BRL/EUR	3.2208	2.8624	2.7086	2.5063
INR/EUR	85.3040	77.6494	72.4638	68.9655
SAR/EUR	5.1532	4.9748	4.9628	4.8216
ILS/EUR*	4.7943	4.7914	-	-

* ADVA Optical Networking Israel Ltd. was acquired on Jan. 2, 2013.

Segment reporting
The internal organizational and management structure and the structure of internal financial reporting activities are the key factors in determining what information is reported. For making decisions about resource allocation and performance assessment, management does not monitor the operating results separately on the level of business units. The Group operates in one business segment only, namely the development, marketing and sale of optical networking solutions.

Cash and cash equivalents
Cash and cash equivalents as reported in the consolidated cash flow statement include short-term liquidity, i.e., cash and cash equivalents and short-term investments and securities with an initial time to maturity not exceeding three months.

Financial assets
Financial assets within the scope of IAS 39 are either classified as financial assets at fair value, affecting the income statement, loans and receivables, investments held to maturity, financial assets available for sale or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The Group determines the classification of its financial assets at initial recognition.

All regular purchases and sales of financial assets are recognized on the trade date, i.e., the date ADVA Optical Networking committed to purchase the asset. Investments are initially recognized at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognized at fair value, and transaction costs are expensed in the income statement.

The Group's financial assets include cash and short-term deposits, trade and other receivables, quoted financial instruments and derivative financial instruments

Subsequent measurement
The subsequent measurement of financial assets depends on their classification as follows:

Financial assets at fair value through profit or loss
Financial assets at fair value through profit or loss include financial assets designated upon initial recognition at fair value through profit or loss. This category includes derivative financial instruments entered into by the Group that are not designated as hedging instruments in hedge relationships as defined by IAS 39. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments. Financial assets at fair value through profit or loss are carried in the statement of financial position at fair value with changes in fair value recognized in other financial gains and losses, net, in the income statement.

For its financial assets at fair value through profit or loss, ADVA Optical Networking evaluates whether the intent to sell them in the near-term is still appropriate or not. When the Group is unable to trade these financial assets due to inactive markets and management's intent to sell them in the foreseeable future significantly changes, in rare circumstances the Group may elect to reclassify these financial assets. The reclassification to loans and receivables, available-for-sale or held to maturity depends on the nature of the asset. This reclassification does not affect the evaluation of financial assets designated at fair value through profit or loss using the fair value option at designation.

The Group has not designated any financial assets upon initial recognition as at fair value through profit or loss.

Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, loans and receivables are subsequently carried at amortized cost using the effective interest rate method less allowances for impairment. Amortized cost is calculated considering any discount or premium at the time of the purchase. The amortized cost includes any fees that are an integral part of the effective interest rate and of the transaction costs. Gains and losses are recognized in the income statement at the time the loans and receivables are written off or impaired.

Held-to-maturity investments
Non-derivative financial assets with fixed or determinable payments and fixed maturities are classified as held-to-maturity when the Group has the positive intention and ability to hold them to maturity. After initial measurement, held-to-maturity investments are measured at amortized cost using the effective interest method, less impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the effective interest rate. The effective interest rate amortization and losses arising from impairment are recognized in the income statement in other financial gains and losses, net.

Available-for-sale investments
The Group did not have any available-for-sale investments during the years ended December 31, 2013 and 2012.

Derecognition
ADVA Optical Networking derecognizes a financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) when:

- The rights to receive cash flows from the asset have expired.

- The Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a "pass-through" arrangement; and either (a) the Group has transferred substantially all the risks and rewards of the asset, or (b) the Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset or has entered into a "pass-through" arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Group's continuing involvement in the asset. In that case, the Group also recognizes an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to repay.

Impairment of financial assets
On each balance sheet date, ADVA Optical Networking assesses whether a financial asset is impaired. If there is objective evidence that an impairment loss on loans and receivables has been incurred, the amount of the loss is determined as the difference between the carrying amount of the financial asset and the present value of expected future cash flows. Impairment losses are recognized in the income statement.

If the amount of the impairment loss decreases in subsequent periods, and provided that the decrease can be related to an event that had occurred after the impairment was recognized, the previously recognized impairment loss is reversed. The loss can only be reversed to the extent that the carrying value of the asset does not exceed its amortized cost on the date of impairment. Any subsequent reversal of an impairment loss affects the income statement.

For trade receivables, a provision for impairment is made, provided that there is objective evidence that ADVA Optical Networking will not be able to collect the full amount due under the original terms of the invoice. The carrying amount of the receivable is reduced through use of an allowance account. Impaired trade receivables are derecognized when they are assessed as uncollectible.

Inventories
Inventories are valued at the lower of cost or net realizable value. The cost of purchase is determined at average prices. Production costs include direct unit costs, an appropriate portion of necessary manufacturing overheads and production-related depreciation that can be directly assigned to the production process. Administrative and social insurance charges that can be assigned to production are also taken into account. Financing charges are not classified as part of the at-cost base. The net realizable value is the estimated selling price that could be realized on the closing date in the context of ordinary business activity, less estimated costs of completion and costs necessary to make the sale.

Inventory depreciation covers risks relating to slow-moving items or technical obsolescence. Where the reasons for previous write-downs no longer apply, those write-downs are reversed.

Property, plant and equipment
Property, plant and equipment is stated at historic cost less accumulated depreciation and accumulated impairment losses, if any. The present value of the expected cost for the decommissioning of the asset after its use is included in the cost of the respective asset if the recognition criteria for a provision are met.

Depreciation on property, plant and equipment is calculated on a straight-line basis over the estimated useful economic lives of the assets as follows:

• Buildings	20 to 25 years
• Technical equipment and machinery	3 to 4 years
• Factory and office equipment	3 to 10 years

Leasehold improvements and other subsidies received under new or renewed operating lease contracts are accounted for according to SIC 15 (Operating leases – incentives). The benefit is recognized as a reduction of the rental expense over the contractual lease term. Leasehold improvements are capitalized as tangible assets and depreciated over the term of the lease on a straight-line basis.

An item of property, plant and equipment is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the income statement when the asset is derecognized.

The assets' residual values, useful economic lives and methods of depreciation are reviewed at each financial year-end, and adjusted prospectively, if appropriate.

Borrowing costs directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalized as part of the cost of the respective assets. If borrowing costs cannot be directly attributed to the acquisition, construction or production of an asset, an assessment is made on whether general borrowing costs should be recognized that would have been avoided if the asset was not acquired, constructed or produced. All other borrowing costs are expensed in the period they occur. Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds.

Intangible assets
Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value on the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses. Internally generated intangible assets, excluding capitalized development costs, are not capitalized, and expenditure is reflected in profit or loss in the year in which the expenditure is incurred.

The useful economic lives of intangible assets are assessed to be either finite or indefinite.

Intangible assets with finite lives are amortized on a straight-line basis over the expected useful economic lives of the assets as follows:

• Capitalized development projects	3 to 5 years
• Purchased technology	5 to 9 years
• Software and other intangible assets	3 to 6 years

Intangible assets with finite useful economic lives are assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life are reviewed at least at each financial year-end. The amortization expense on intangible assets with finite lives is recognized in profit or loss in the expense category consistent with the function of the intangible asset. Amortization of purchased intangible assets and amortization of capitalized development projects is recognized in profit or loss in the positions stated in note (11).

Intangible assets with an indefinite useful life are not amortized. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether the indefinite life assessment continues to be applicable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis. There are no intangible assets with indefinite lives other than goodwill.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the fair value less costs to sell and the carrying amount of the asset, and they are recognized in the income statement when the asset is derecognized.

Impairment test for intangible assets
Intangible assets with indefinite useful economic lives are tested for impairment annually and whenever there is an indication for potential impairment, either individually or at the cash generating unit level.

Goodwill
An unlimited useful life is assumed for goodwill acquired in the context of business combinations. Impairment reviews are performed at the cash generating unit level on the balance sheet date or when there is an indication that the goodwill may be impaired in accordance with IAS 36. Impairment losses on goodwill recognized in prior periods are not reversed. See note (11).

Purchased technology
Purchased technology has a finite useful life. It is stated at cost and amortized on a straight-line basis over estimated useful economic lives of five to nine years. It is tested for impairment if an indication exists that the recoverable amount of the asset may have decreased.

Capitalized development projects
Development expenses for new products are capitalized as development projects if
- they can be unambiguously assigned to those products,
- the products under development are technically feasible and can be marketed,
- there is reasonable certainty that the development activity will result in future cash inflows, and
- ADVA Optical Networking intends and is able to complete and use the development project.

Capitalized development projects include all costs that can be directly assigned to the development process. Financing charges are capitalized if the development project represents a qualifying asset in the sense of IAS 23.

After initial recognition of a development project as an asset, measurement is at historical cost, less accumulated amortization and impairment. The straight-line method of amortization is used from the start of production through the estimated selling periods for the products developed (generally between three and five years). Completed as well as ongoing development projects are tested for impairment on the balance sheet date or when there is an indication of potential impairment. Impairment losses are recognized if appropriate.

Research costs are expensed as incurred according to IAS 38.

Government grants
Government grants are recognized where there is reasonable assurance that the grant will be received and all attached conditions will be met. When the grant relates to an expense item, it is recognized as income over the period necessary to match the grant on a systematic basis to the costs that it is intended to compensate. Where the grant relates to an asset, it is recognized as a reduction of purchase costs and released as a reduction of depreciation expense over the expected useful life of the related asset.

Leasing
Leasing contracts are classified as finance leases if substantially all risks and rewards, and with it the economic ownership, are transferred to the lessee. All other leasing transactions are classified as operating leases.

Property, plant and equipment acquired by ADVA Optical Networking through finance lease contracts is stated at the fair value of the leased property or, if lower, the present value of the future minimum lease payments when the contract commences. Finance lease contracts are then amortized using the straight-line method over the shorter of the leasing period or the estimated useful life of the assets. The correspondent liability is shown as finance lease obligation. The lease payment to the lessor is apportioned between finance charge and the reduction of the outstanding liability. The finance charge is allocated to each period during the lease term to produce a constant periodic rate of interest on the remaining liability.

Operating lease payments are recognized as an expense in the income statement on a straight-line basis over the lease term.

Financial liabilities

Initial recognition and measurement

Financial liabilities within the scope of IAS 39 are classified as financial liabilities at fair value through profit or loss, loans and borrowings, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The Group determines the classification of its financial liabilities at initial recognition. All financial liabilities are recognized initially at fair value. Loans and borrowings are recognized net of directly attributable transaction costs.

ADVA Optical Networking's financial liabilities include trade and other payables, bank overdrafts, loans and borrowings and derivative financial instruments.

Subsequent measurement

The measurement of financial liabilities depends on their classification as follows:

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss include financial liabilities designated upon initial recognition as at fair value through profit or loss. Financial liabilities are classified as held for trading if they are acquired for selling in the near-term. This category includes derivative financial instruments entered into by the Group that are not designated as hedging instruments in hedge relationships as defined by IAS 39. Separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Gains or losses on liabilities held for trading are recognized in the income statement. ADVA Optical Networking has not designated any financial liabilities upon initial recognition as at fair value through profit or loss.

Loans and borrowings

After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortized cost using the effective interest rate method. Gains and losses are recognized in the income statement when the liabilities are derecognized as well as through the effective interest rate method (EIR) amortization process. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortization is included in interest expenses in the income statement.

Derecognition

A financial liability is derecognized when the obligation under the liability is discharged, cancelled or expires. When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability. The difference in the respective carrying amounts is recognized in the income statement.

Provisions
Provisions are recognized when the Group has a present obligation (legal or constructive) as a result of a past event, when it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Where the Group expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognized as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in profit or loss, net of any reimbursement. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision over time is recognized in other financial gains and losses, net.

Derivative financial instruments and hedging activities
The Group entered into forward rate agreements to hedge foreign currency exposure of expected future cash flows. These derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently re-measured at their fair value through profit or loss.

The Group did not apply hedge accounting rules according to IAS 39 during the years ended December 31, 2013 and 2012.

Revenue recognition
Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received or receivable, net of discounts, rebates and other sales taxes or duty. The following specific recognition criteria must also be met before revenue is recognized:

Sale of goods
Revenue from the sale of goods is recognized when the significant risks and rewards of ownership of the goods have passed to the buyer, usually on delivery of the goods.

Product returns that are estimated according to contractual obligations and past revenues statistics are recognized as a reduction of revenues.

Rendering of services
Revenues arising from the sale of services primarily derive from training, maintenance and installation services and are recognized when those services have been rendered. Installation services are recognized as revenue if the customer has approved the final installation. Generally, maintenance services are reported as deferred revenue and recognized as revenue straight-line over the contract period. Training is recognized as revenue immediately after rendering of the service.

In arrangements with a customer that include delivery of goods as well as rendering of services, the shipment of the goods is separated from the rendering of the services if the goods have a stand-alone value for the customer and the fair value of the service can be reliably determined. Both components of the transaction are measured at their respective fair value.

Cost of goods sold
The cost of goods sold comprises the costs incurred in the production and rendering of services. This item subsumes both the direct cost of materials and production directly assignable to a product and indirect (overhead) costs, including the depreciation of production equipment, amortization of production related intangible assets and write-downs on inventories. The cost of goods sold also includes appropriation to the warranty provision. Income from the reversal of write-downs on inventories reduces the cost of goods sold, which also includes amortization of purchased technologies.

Interest income and expenses
For all financial instruments measured at amortized cost and interest-bearing financial assets classified as available-for-sale, interest income or expenses are recorded using the effective interest rate, which is the rate that exactly discounts the estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or liability.

Taxes
Current income tax
Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted on the respective balance sheet date.

Deferred income tax
Deferred tax is provided using the liability method on temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax liabilities are recognized for all taxable temporary differences, except:

- where the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect to taxable temporary differences associated with investments in subsidiaries, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the near future.

Deferred tax assets are recognized for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilized, except:

- where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and

- in respect of deductible temporary differences associated with investments in subsidiaries, deferred tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

The carrying amount of deferred tax assets is reviewed on each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. Unrecognized deferred tax assets are reassessed on each balance sheet date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be utilized.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted on the balance sheet date. Future changes in tax rates are recognized on the balance sheet date if their impact is materially certain as part of the tax legislation process.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Share-based compensation transactions

Employees (including senior executives) of ADVA Optical Networking receive remuneration in the form of share-based compensation transactions, whereby employees render services as consideration for equity instruments (equity-settled transactions) or they are granted stock appreciation rights, which are settled in cash (cash-settled transactions). Share-based compensation transactions are reported and valued in accordance with IFRS 2.

Share-based compensation transactions between different entities of ADVA Optical Networking are considered as either equity-settled or cash-settled share-based compensation transactions in the individual financial statements of ADVA Optical Networking SE. The Group entities employing the beneficiaries measure the received services as an equity-settled share-based compensation transaction. No repayment arrangements have been set up between the entities of ADVA Group.

Equity-settled transactions

The cost of equity-settled transactions with employees is measured by reference to the fair value on the grant date. The fair value is determined by an external expert using an appropriate pricing model. See note (31) for further details.

The cost of equity-settled transactions is recognized, together with the corresponding increase in equity, over the period in which the relevant employees become fully entitled to the award (vesting date). No expense is recognized for awards that do not ultimately vest, except for awards where vesting is conditional upon market condition, which are treated as vesting irrespective of whether or not market condition is satisfied, provided that all other performance conditions are satisfied.

Where the terms of an equity-settled transaction award are modified, the minimum expense recognized is the expense as if the terms had not been modified, if the original terms of the award are met. An additional expense is recognized for any modification that increases the total fair value of the share-based compensation transaction, or is otherwise beneficial to the employee as measured on the date of modification.

Where an equity-settled award is cancelled, it is treated as if it vested on the date of cancellation, and any expense not yet recognized for the award is recognized immediately. This includes any award where non-vesting conditions within the control of either the entity or the employee are not met. However, if a new award is substituted for the cancelled award, and designated as a replacement award on the date that it is granted, the cancelled and new awards are treated as if they were a modification of the original award, as described in the previous paragraph. All cancellations of equity-settled transactions are treated equally.

The dilutive effect of outstanding options is reflected in the computation of earnings per share. See note (24).

Cash-Settled Transactions
The cost of cash-settled transactions is measured initially at fair value on the grant date. The fair value is expensed over the vesting period with recognition of a corresponding provision. The provision is re-measured on each balance sheet date up to and including the settlement date, with changes in the fair value recognized in profit or loss.

Earnings per share
The Group calculates basic and diluted earnings per share in accordance with IAS 33. Basic earnings per share are calculated based on the weighted average number of no-par value shares outstanding during the reporting period. Diluted earnings per share are calculated based on the weighted average number of no-par value shares outstanding during the reporting period, but also including the number of no-par value shares that could come into existence if all stock options were exercised on the balance sheet date.

(5) Significant Accounting Judgments, Estimates and Assumptions

The preparation of the Group's financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities and the disclosure of contingent liabilities on the reporting date. However, uncertainty about these assumptions and estimates could result in outcomes that could require a material adjustment to the carrying amount of the asset or liability affected in the future. Assumptions used to make estimates are regularly reviewed. Changes in estimates only affecting one accounting period are only taken into account in that accounting period. In the case of changes in estimates that affect the current and future accounting periods, these are taken into account appropriately in the current and subsequent accounting periods.

Discussed below are the key judgments and assumptions concerning the future and other key sources of estimation and uncertainty on the balance sheet date that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Impairment of non-financial assets

The Group assesses whether there are any indicators of impairment for all non-financial assets on each reporting date. Goodwill and other indefinite life intangibles are tested for impairment annually and at other times when such indicators exist. Other non-financial assets are tested for impairment when there are indicators that the carrying amounts may not be recoverable. When value-in-use calculations are undertaken, management must estimate the expected future cash flows from the asset or cash generating unit and choose a suitable discount rate in order to calculate the present value of those cash flows. See note (11) for the carrying amounts involved.

Taxes

Uncertainties exist with respect to the interpretation of complex tax regulations and the amount and timing of future taxable income. Given the wide range of international business relationships and the long-term nature and complexity of existing contractual agreements, differences arising between the actual results and the assumptions made, or future changes to such assumptions, could necessitate future adjustments to tax income and expenses already recorded. The Group establishes provisions, based on reasonable estimates, for possible consequences of audits by the tax authorities of the respective countries in which it operates. The amount of such provisions is based on various factors, such as experience of previous tax audits and differing interpretations of tax regulations by the taxable entity and the responsible tax authority. Such differences of interpretation may arise on a wide variety of issues depending on the conditions prevailing in the respective Group company's domicile.

Deferred tax assets are recognized for all unused tax losses to the extent that it is probable that taxable profit will be available to utilize those losses. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and level of future taxable profits together with future tax planning strategies. See note (22) for the carrying amounts involved.

Development expenses

Development expenses are capitalized in accordance with the accounting policy described in note (4). Initial capitalization of costs is based on management's judgment that technological and economic feasibility is confirmed, usually when a product development project has reached a defined milestone according to an established project management model. In determining the amounts to be capitalized, management makes assumptions regarding the expected future cash generation of the assets, discount rates to be applied and the expected period of benefits. See note (11) for the carrying amounts involved.

Provisions

Significant estimates are involved in the determination of provisions related to warranty costs and legal proceedings. The estimate of warranty claims is based on historic data and is extrapolated into the future. Legal proceedings often involve complex legal issues and are subject to substantial uncertainties. Accordingly, management exercises considerable judgment in determining whether there is a present obligation as a result of a past event at the end of the reporting period, whether it is more likely than not that such a proceeding will result in an outflow of resources and whether the amount of the obligation can be reliably estimated. Provisions are described in note (15).

Share-based compensation transactions

The Group measures the cost of equity-settled and cash-settled transactions with employees by reference to the fair value of the equity instruments on the date at which they are granted or on the balance sheet date. Estimating fair value requires determining the most appropriate valuation model for a grant of equity instruments, which is dependent on the terms and conditions of the grant. This also requires determining the expected life of the option, volatility and dividend yield, as well as further assumptions. See note (31) for the carrying amounts involved.

(6) Scope of Consolidation and Shareholdings

The consolidated financial statements for the year ended on December 31, 2013, include the financial statements of ADVA Optical Networking SE plus all of the 14 (13 on December 31, 2012) wholly-owned subsidiaries listed below (hereafter collectively referred to as "the Group companies"):

(in thousands)			Equity	Net income (loss)	Share in equity owned directly	Share in equity owned in-directly
ADVA Optical Networking North America, Inc., Norcross/Atlanta (Georgia), USA	USD	*	43,722	1,642	100%	-
ADVA Optical Networking Ltd., York, United Kingdom	GBP	**	4,465	-432	100%	-
ADVA Optical Networking AS, Oslo, Norway	NOK	**	21,178	2,134	100%	-
ADVA Optical Networking AB, Kista/Stockholm, Sweden	SEK	**	5,056	116	100%	-
ADVA Optical Networking Serviços Ltda., São Paulo, Brazil	BRL	*	574	125	99%	1%
ADVA Optical Networking (Shenzhen) Ltd., Shenzhen, China	CNY	**	31,065	5,798	100%	-
ADVA Optical Networking Singapore Pte. Ltd., Singapore	SGD	**	2,389	106	100%	-
ADVA Optical Networking Hong Kong Ltd., Hong Kong, China	HKD	**	430	89	-	100%
ADVA Optical Networking Corp., Tokyo, Japan	JPY	*	77,396	-570	100%	-
ADVA Optical Networking sp. z o.o., Gdynia, Poland	PLN	**	4,590	1,739	100%	-
ADVA Optical Networking (India) Private Ltd., Bangalore, India	INR	***	6,126	4,084	1%	99%
ADVA Optical Networking LLC., Riyadh, Kingdom of Saudi Arabia	SAR	*	221	-6	95%	5%
ADVA Optical Networking Trading (Shenzhen) Ltd., Shenzhen, China	USD	*	468	36	-	100%
ADVA Optical Networking Israel Ltd., Ra'anana/Tel Aviv, Israel	ILS	*	10,179	1,053	100%	-

* Prepared in accordance with the International Financial Reporting Standards (IFRS) for the financial year ended December 31, 2013.
** Prepared in accordance with local commercial law for the financial year ended December 31, 2012.
*** Prepared in accordance with local commercial law for the financial year ended March 31, 2013.

ADVA Optical Networking North America, Inc. (ADVA Optical Networking North America) is a R&D, production, sales and administration site with locations in Norcross (Georgia), Paramus (New Jersey) and Richardson (Texas), USA.

ADVA Optical Networking Ltd. (ADVA Optical Networking York) is a logistics and sales site in York, United Kingdom.

ADVA Optical Networking AS (ADVA Optical Networking Oslo) is a R&D site in Oslo, Norway. At the end of 2013, the Management decided to close the site within the next six months.

ADVA Optical Networking AB, Kista/Stockholm, Sweden, (ADVA Optical Networking Stockholm) is responsible for sales in Scandinavia.

ADVA Optical Networking Serviços Ltda., São Paulo, Brazil, (ADVA Optical Networking São Paulo) is a sales office for the Latin America region.

ADVA Optical Networking (Shenzhen) Ltd. (ADVA Optical Networking Shenzhen) is a Chinese R&D and administration site in Shenzhen, China.

ADVA Optical Networking Singapore Pte. Ltd. (ADVA Optical Networking Singapore) is a sales office for the Asia-Pacific region, excluding Japan and South Korea. ADVA Optical Networking Singapore has three subsidiaries: in Bangalore, India, ADVA Optical Networking (India) Private Ltd., in Hong Kong, China, ADVA Optical Networking Hong Kong Ltd. and in Shenzhen, China, ADVA Optical Networking Trading (Shenzhen) Ltd.

ADVA Optical Networking Corp. (ADVA Optical Networking Tokyo) is responsible for sales in Japan and South Korea.

ADVA Optical Networking sp. z o.o. (ADVA Optical Networking Gdynia) is a R&D and administration site in Poland.

ADVA Optical Networking (India) Private Ltd., Bangalore, India, (ADVA Optical Networking Bangalore) is responsible for sales in the Indian sub-continent.

ADVA Optical Networking LLC., Riyadh, Kingdom of Saudi Arabia (ADVA Optical Networking Riyadh) is responsible for the sales activities in the Middle East. In October 2013, the Management decided to close the entity.

ADVA Optical Networking Trading (Shenzhen) Ltd. (ADVA Optical Networking Trading) is a logistics site in Shenzhen, China.

Investments in associates and joint ventures
ADVA Optical Networking North America has a 44.5% share in OptXCon Inc., Raleigh (North Carolina), USA. The Company concluded operations in 2002. The investment is fully depreciated. There are no local financial statements available.

After deletion of the company in the commercial register in 2013 the 45% share of ADVA Optical Networking SE in “Island House Trading 32 (Pty) Ltd. trading as Khanyisa Optical Networking (Pty) Ltd.”, Pretoria, South Africa, with the book value of EUR 1 thousand has been derecognized.

ADVA Optical Networking SE holds 10% of the shares of Saguna Networks Ltd., Nesher, Israel. Due to contractually guaranteed veto rights as well as the nomination of a board member of the company, ADVA Optical Networking SE has significant influence on the business activities of Saguna Networks Ltd. The investment has a nominal value of USD 1,000 thousand (EUR 782 thousand). Due to the fact that at the time of completion of the consolidated financial statements no local audited financial statements 2013 were available for Saguna Networks Ltd., the associate has been recognized at amortized cost. A service agreement exists between the Group and its associate undertaking regarding the provision of development services. In 2013, the Company paid out a loan in the amount of USD 310 thousand (EUR 229 thousand) to Saguna Networks Ltd., Nesher, Israel. The loan is due to be repaid within the next two years.

Changes in scope of consolidation

Acquisition of Biran High-Tech Advisors Ltd
In order to further enhance its Carrier Ethernet engineering capabilities, ADVA Optical Networking SE acquired 100% of the share capital of Biran High-Tech Advisors Ltd, Ra'anana/Tel Aviv, Israel by means of a share deal, on January 2, 2013. The total purchase price amounted to USD 2,915 thousand (EUR 2,213 thousand) and was paid out in two installments in January and April 2013, respectively. In addition, USD 300 thousand (EUR 227 thousand) were paid to a key employee for his share in the developed technology.

Biran High-Tech Advisors Ltd changed its name to ADVA Optical Networking Israel Ltd. (ADVA Optical Networking Israel) on March 20, 2013.

The purchase price allocation according to IFRS 3 performed on January 2, 2013, included in the consolidated financial statements incorporates the cash considerations paid in January and April 2013. During the course of the consolidation, purchased technology was recognized. The remaining excess purchase price is classified as goodwill and represents the fair value of anticipated synergies from the acquisition as well as the assembled workforce of ADVA Optical Networking Israel. No further fair value adjustments of assets, liabilities and contingent assets acquired applied. The goodwill is not tax deductible.

The expected remaining useful life of the purchased technology is 5 years.

The fair values of acquired assets and liabilities at the date of the acquisition and carrying amounts immediately prior to the date of the acquisition comprise as follows:

(in thousands of EUR)	Carrying amount	Fair value at the date of the acquisition
Cash and cash equivalents	2,734	2,734
Property, plant and equipment	250	250
Purchased technology	-	455
Other current and non-current assets	52	52
Current and non-current liabilities	-1,214	-1,214
Deferred tax liability	-	-114
Net assets	**1,822**	**2,163**
Goodwill	**-**	**277**
Total purchase price	**-**	**2,440**

The net cash inflow from the acquisition comprises as follows:

(in thousands of EUR)	
Cash and cash equivalents acquired from ADVA Optical Networking Israel	2,734
Cash paid on acquisition	-2,440
Net cash inflow from acquisition	**294**

From the date of the acquisition, ADVA Optical Networking Israel has contributed EUR 150 thousand to the net profit of the Group. The entity does not generate third-party revenues.

(7) Cash and Cash Equivalents

Cash and cash equivalents on December 31 include the following amounts to which ADVA Optical Networking has only limited access:

(in thousands of EUR)	2013	2012
Amounts pledged as security	324	351

Cash at banks earns interest at floating rates based on daily bank deposit rates.

Cash equivalents are invested for varying periods of between one day and three months, depending on the immediate cash requirements of the Group, and earn interest at the respective short-term deposit rates.

On December 31, 2013, the Group had EUR 8,000 thousand (on December 31, 2012: EUR 8,000 thousand) of undrawn committed borrowing facilities available in respect of which all conditions had been met.

(8) Trade Accounts Receivable

Trade accounts receivable are non-interest-bearing and are due within 30 to 120 days in general. For specific projects, other payment terms may be agreed.

Gross trade accounts receivable and depreciation of trade accounts receivable have developed as follows:

(in thousands of EUR)	2013	2012
Gross trade accounts receivable	**53,411**	**57,699**
Depreciation		
On January 1	2,235	374
Increase	557	2,122
Usage	-1,641	0
Release	-474	-261
Exchange rate differences	-5	0
On December 31	**672**	**2,235**
Net trade accounts receivable	**52,739**	**55,464**

On December 31, 2013 and 2012, there was no material off balance sheet credit risk. See note (27) for further disclosures.

Depreciation of trade accounts receivable is based on an assessment of balances past their due date. Trade accounts receivable past due analyzes as follows:

(in thousands of EUR, on December 31)	2013 gross value	2013 depreciation	2012 gross value	2012 depreciation
Less than 3 months	4,798	-	4,841	865
3 to 6 months	416	176	1,515	740
6 to 12 months	111	111	492	313
More than 1 year	385	385	317	317
	5,710	**672**	**7,165**	**2,235**

On December 31, 2013, EUR 5,038 thousand of trade receivables are past due but not impaired (prior year: EUR 4,751 thousand). Trade accounts receivable that are not overdue were not impaired in 2013 and 2012, respectively.

A Group company entered into a supplier finance agreement, whereby it can finance receivables from a specific customer for a period of up to 120 days. Credit risks and settlement risks are transferred to the financing institution. The Group paid an annual fee amounting to LIBOR plus 0.92% for transactions until August 31, 2013 and LIBOR plus 0.75% from September 1, 2013 on the volume of receivables transferred. In 2013, the Group incurred interest expenses of EUR 194 thousand pertaining to this arrangement (prior year: EUR 200 thousand).

Another Group company entered into three supplier finance agreements. The agreements entitle the Group company to finance receivables from a specific customer with a maturity of minimum 45 days. ADVA Optical Networking pays annual interest amounting to EURIBOR plus 3% on the volume of the receivables transferred. In addition, a service charge of EUR 500 per transaction applies. In 2013, ADVA Optical Networking SE incurred interest expenses of EUR 115 thousand (prior year: EUR 211 thousand) pertaining to this agreement. These agreements will terminate on April 30, 2014.

(9) Inventories

The table below summarizes the composition of inventories on December 31:

(in thousands of EUR)	2013	2012
Raw materials and supplies	9,977	7,338
Work in progress	2,361	2,798
Finished goods	27,736	31,203
	40,074	**41,339**

In 2013, depreciation of inventories amounting to EUR 2,211 thousand (prior year: EUR 4,466 thousand) was recognized as an expense within cost of goods sold. This amount includes reversals of earlier write-downs in the amount of EUR 313 thousand (prior year: EUR 422 thousand) due to higher selling and input prices.

In 2013 and 2012, material costs of EUR 136,115 thousand and EUR 144,751 thousand, respectively, have been recognized.

(10) Other Current and Non-Current Assets

On December 31, other current assets can be analyzed as follows:

(in thousands of EUR)	2013	2012
Prepaid expenses	1,422	1,819
Receivables due from tax authorities	303	457
Positive fair values of derivative financial instruments	-	48
Government grant allowances for research projects	2,662	3,408
Other	264	1,002
	4,651	**6,734**

Other current assets are non-interest-bearing and are generally due within 0 to 60 days. Further disclosures on derivative financial instruments are given in note (21).

Other non-current assets include mainly lease deposits of EUR 787 thousand (prior year: EUR 795 thousand) and non-current claims from government grant allowances for research projects of EUR 965 thousand (prior year: EUR 1,431 thousand).

On December 31, 2013, government grants for eleven research projects are recognized (December 31, 2012: nine research projects). These public grants relate to programs promoted by the EU and national governments.

(11) Fixed Assets

The following changes in fixed assets were recorded in 2013 and 2012:

(in thousands of EUR)	Historical cost							Accumulated depreciation							Net book values	
	Jan. 1, 2013	Additions	Disposals/retirements	Reclassifications	Currency translation adjustments	Change in scope of consolidation	Dec. 31, 2013	Jan. 1, 2013	Depreciation of the period	Depreciation on disposals/retirements	Reclassifications	Currency translation adjustments	Change in scope of consolidation	Dec. 31, 2013	Dec. 31, 2013	Dec. 31, 2012
Finance leases	**2,670**	**-**	**-67**	**-**	**-2**	**-**	**2,601**	**2,619**	**15**	**-49**	**-**	**-**	**-**	**2,585**	**16**	**51**
Property, plant and equipment																
Land and buildings	11,958	236	-	19	-83	18	12,148	4,565	800	-	-	-38	2	5,329	6,819	7,393
Technical equipment and machinery	52,368	5,802	-1,409	319	-998	281	56,363	38,813	6,205	-1,124	-	-800	152	43,246	13,117	13,555
Factory and office equipment	9,843	886	-145	10	-157	178	10,615	7,931	1,026	-118	-	-133	73	8,779	1,836	1,912
Assets under construction	427	65	-38	-348	-12	-	94	-	-	-	-	-	-	-	94	427
	74,596	**6,989**	**-1,592**	**-**	**-1,250**	**477**	**79,220**	**51,309**	**8,031**	**-1,242**	**-**	**-971**	**227**	**57,354**	**21,866**	**23,287**
Intangible assets																
Goodwill	74,627	-	-	-	-1,399	277	73,505	54,751	-	-	-	-1,121	-	53,630	19,875	19,876
Capitalized development projects	105,588	22,490	-	-	-410	-	127,668	58,091	17,759	-	-	-262	-	75,588	52,080	47,497
Purchased technology	29,946	-	-	-	-799	455	29,602	28,761	641	-	-	-812	-	28,590	1,012	1,185
In-process development projects	2,194	-	-	-	-90	-	2,104	2,194	-	-	-	-90	-	2,104	-	-
Other intangible assets	53,522	698	-7	-	-326	-	53,887	51,121	1,491	-7	-	-405	-	52,200	1,687	2,401
	265,877	**23,188**	**-7**	**-**	**-3,024**	**732**	**286,766**	**194,918**	**19,891**	**-7**	**-**	**-2,690**	**-**	**212,112**	**74,654**	**70,959**
Financial investments																
Investments in associates and joint ventures	1,746	-	-1	-	-39	-	1,706	963	-	-	-	-39	-	924	782	783
Loans to investments in associates and joint ventures	-	229	-	-	-	-	229	-	-	-	-	-	-	-	229	-
	1,746	**229**	**-1**	**-**	**-39**	**-**	**1,935**	**963**	**-**	**-**	**-**	**-39**	**-**	**924**	**1,011**	**783**
	344,889	**30,406**	**-1,667**	**-**	**-4,315**	**1,209**	**370,522**	**249,809**	**27,937**	**-1,298**	**-**	**-3,700**	**227**	**272,975**	**97,547**	**95,080**

(in thousands of EUR)	Historical cost						Accumulated depreciation						Net book values	
	Jan. 1, 2012	**Additions**	**Disposals/ retirements**	**Reclassifications**	**Currency translation adjustments**	**Dec. 31, 2012**	**Jan. 1, 2012**	**Depreciation of the period**	**Depreciation on disposals/ retirements**	**Reclassifications**	**Currency translation adjustments**	**Dec. 31, 2012**	**Dec. 31, 2012**	**Dec. 31, 2011**
Finance leases	**2,750**	**25**	**-109**	**-**	**4**	**2,670**	**2,701**	**26**	**-109**	**-**	**1**	**2,619**	**51**	**49**
Property, plant and equipment														
Land and buildings	11,707	272	-	-	-21	11,958	3,832	740	-	-	-7	4,565	7,393	7,875
Technical equipment and machinery	51,353	7,796	-7,336	628	-73	52,368	40,519	5,628	-7,198	-	-136	38,813	13,555	10,834
Factory and office equipment	9,820	705	-719	3	34	9,843	7,589	1,024	-703	-	21	7,931	1,912	2,231
Assets under construction	659	394	-	-631	5	427	-	-	-	-	-	-	427	659
	73,539	**9,167**	**-8,055**	**-**	**-55**	**74,596**	**51,940**	**7,392**	**-7,901**	**-**	**-122**	**51,309**	**23,287**	**21,599**
Intangible assets														
Goodwill	73,825	-	-	-	802	74,627	53,983	-	-	-	768	54,751	19,876	19,842
Capitalized development projects	81,898	23,509	-	-	181	105,588	42,667	15,394	-	-	30	58,091	47,497	39,231
Purchased technology	30,358	-	-	-	-412	29,946	27,674	1,506	-	-	-419	28,761	1,185	2,684
In-process development projects	2,239	-	-	-	-45	2,194	2,239	-	-	-	-45	2,194	-	-
Other intangible assets	53,218	1,503	-1,238	-	39	53,522	50,361	1,964	-1,238	-	34	51,121	2,401	2,857
	241,538	**25,012**	**-1,238**	**-**	**565**	**265,877**	**176,924**	**18,864**	**-1,238**	**-**	**368**	**194,918**	**70,959**	**64,614**
Financial investments														
Investments in associates and joint ventures	983	782	-	-	-19	1,746	982	-	-	-	-19	963	783	1
	983	**782**	**-**	**-**	**-19**	**1,746**	**982**	**-**	**-**	**-**	**-19**	**963**	**783**	**1**
	318,810	**34,986**	**-9,402**	**-**	**495**	**344,889**	**232,547**	**26,282**	**-9,248**	**-**	**228**	**249,809**	**95,080**	**86,263**

Finance leases
The Group has financial obligations arising from a variety of finance lease agreements for factory and office equipment.

Further information on leases as well as the costs and minimum future lease payments arising from these leases are listed under note (12).

Property, plant and equipment
The classification and changes in property, plant and equipment are shown in the analysis of changes in fixed assets.

In 2013 and 2012, there were neither impairments nor write-backs of property, plant and equipment impaired in prior years.

In 2013, the Group received government grants of EUR 414 thousand (prior year: EUR 241 thousand) for property, plant and equipment. Based on grant allowances EUR 420 (prior year: nil) allowances have been deducted from historical costs in 2013.

Goodwill
The table below shows the composition of goodwill on December 31, as well as the cash-generating unit to which the goodwill is allocated for impairment testing:

(in Tausend EUR)	2013	2012
FirstFibre Ltd. (ADVA Optical Networking York)	6,841	6,841
Cellware GmbH (ADVA Optical Networking SE)	481	481
Covaro Networks Inc. (ADVA Optical Networking York)	10,150	10,150
Movaz Networks Inc. (ADVA Optical Networking North America)	4,448	4,448
Gryfsoft sp. z o.o. (ADVA Optical Networking Gdynia)	130	130
Biran High-Tech Advisors Ltd. (ADVA Optical Networking Israel)	277	-
Effect of foreign currency translation	-2,452	-2,174
	19,875	**19,876**

Impairment of goodwill
In 2013 and 2012, no impairment of goodwill was recognized.

Key assumptions used in impairment testing
For impairment testing purposes, goodwill is generally allocated to the acquired Group companies, respectively. For Covaro Networks Inc. goodwill is allocated to the Group company who owns the respective technology. The Group companies represent the cash generating units.

On December 31, 2013 and 2012, the value in use of the goodwill was calculated based on future cash flows (discounted-cash-flow-method). The calculation is most sensitive to the following assumptions:

- Gross margins
- Discount rates
- Raw material prices
- Market share expected

Cash flows include the projected cash flows for the three subsequent years as per the approved budget and three-year planning for gross margins, market share and raw material prices. For further periods, a perpetual income is estimated based on nil growth with inflation offset. The discount rate used for the calculation is a pre-tax rate, considers the specific risk of each group company and is calculated according to the Capital Asset Pricing Model (CAPM). The cost of equity is composed of a risk-free interest rate and a specific risk mark-up calculated as the difference of the average market rate of return and the risk-free interest rate multiplied with the specific risk related to the Company (beta coefficient). The beta coefficient is calculated on a peer group basis. The calculation uses pre-tax discount rates depending on the different cash generating units.

• Pre-tax discount rate	11.8% to 17.9%
• Risk-free interest rate	2.04% on average
• Risk mark-up	6.0%
• Beta coefficient (weighted average of the peer group)	1.47

Sensitivity analysis
The implications of adverse changes on the key assumptions for the recoverable amount are discussed below. Each key assumption is considered in turn, even though there are dependencies between the assumptions:

- Gross margin – a reduction of more than 1.6 percentage points of the expected average gross margin over the planning period would result in an impairment loss in the unit ADVA Optical Networking Gdynia.

- Discount rate – an increased pre-tax discount rate of more than 2.9 percentage points would result in an impairment loss in the unit ADVA Optical Networking Gdynia.

- Growth rate – a growth reduction of more than 46.9% would result in an impairment loss in the unit ADVA Optical Networking North America.

Capitalized development projects, purchased technology and other intangible assets
The table below summarizes carrying amounts of capitalized development projects, purchased technology and other intangible assets on December 31:

(in thousands of EUR)	2013	2012
Capitalized development projects	52,080	47,497
Purchased technology	1,012	1,185
Other intangible assets	1,687	2,401
	54,779	**51,083**

Capitalized development projects include the development of Ethernet access products amounting to EUR 2,467 thousand (prior year: EUR 5,111 thousand) and of WDM solutions amounting to EUR 49,613 thousand (prior year: EUR 42,386 thousand). The remaining amortization period is between one month and four years.

In 2013 borrowing costs of EUR 163 thousand (2012: EUR 286 thousand) were capitalized related to development projects with an expected duration of more than 12 months. Borrowing costs were capitalized at the weighted average rate of the financial liabilities of 3.5%

Purchased technology includes the capitalized technologies from the acquisitions of Covaro amounting to EUR 638 thousand (prior year: EUR 1,185 thousand) and Biran amounting to EUR 374 thousand (prior year: nil). The net book value of Covaro technology will be fully depreciated in two years (prior year: three years). The net book value of Biran technology will be fully depreciated in four years.

Amortization of intangible assets
Amortization of intangible assets with a finite useful life comprises:

(in thousands of EUR)	2013	2012
Capitalized development projects	17,759	15,394
Purchased technology	641	1,506
Other intangible assets	1,491	1,964
	19,891	**18,864**

In the income statement, amortization of capitalized development projects and amortization of purchased technology is included in line item "Cost of goods sold".

The amortization of purchased technology is related to Covaro and Biran and amounts to EUR 547 thousand and EUR 94 thousand, respectively, (prior year: EUR 547 thousand and EUR nil, respectively). In 2012, amortization of purchased technology included EUR 959 thousand for Movaz technology. The Movaz technology was fully depreciated in 2012.

Impairment of intangible assets
In 2013 and 2012, no impairment of intangible assets with finite useful economic lives was recognized.

The methodology for calculating impairment is the same as the one used for goodwill impairment testing. The key assumptions and key sensitivities are also the same.

Income from capitalization of development expenses, net of amortization for capitalized development projects

(in thousands of EUR)	2013	2012
Income from capitalization of development expenses	22,490	23,509
Amortization of capitalized development projects	-17,759	-15,394
	4,731	**8,115**

In the income statement, amortization of capitalized development projects is included within cost of goods sold. Income from capitalization of development expenses is included in line research and development expenses.

(12) Finance Lease Obligations

The Group has financial obligations arising from a variety of finance lease agreements for factory and office equipment. These obligations will expire at varying times over the next two years.

(in thousands of EUR)	Minimum lease payments Dec. 31, 2013	Minimum lease payments Dec. 31, 2012	Present value of minimum lease payments Dec. 31, 2013	Present value of minimum lease payments Dec. 31, 2012
Up to one year	6	29	5	27
One to five years	9	15	9	14
More than five years	-	-	-	-
	15	**44**	**14**	**41**

(13) Financial Liabilities

The table below details financial liabilities and their maturity:

(in thousands of EUR)	Dec. 31, 2013	Interest terms	Maturity ≤ 12 months	Maturity 13 – 36 months	Maturity > 36 months
IKB Deutsche Industriebank loans*	781**	Fixed rate, subsidized***	313	468	-
	2,083	Fixed rate, subsidized***	833	1,250	-
	24,916	Fixed rate, subsidized***	3,053	12,493	9,370
Portigon AG bonded loan*	11,416	Floating rate based on 3M EURIBOR	-	-	11,416
Total financial liabilities	**39,196**		**4,199**	**14,211**	**20,786**

* Key covenants refer to the Group's year-end debt/equity ratio and to the quarter-end net liquidity.

** At the end of 2013, the IKB Deutsche Industriebank loan is secured by a registered land charge without certificate amounting to EUR 5,581 thousand (end of 2012: EUR 5,581 thousand) on the production and development site in Meiningen.

*** Subsidized by the German Reconstruction Loan Company (Kreditanstalt für Wiederaufbau, KfW).

(in thousands of EUR)	Dec. 31, 2012	Interest terms	Maturity ≤ 12 months	Maturity 13 – 36 months	Maturity > 36 months
IKB Deutsche Industriebank loans*	1,094**	Fixed rate, subsidized***	312	625	157
	2,500	Fixed rate, subsidized***	417	1,667	416
IKB Deutsche Industriebank bonded loan*	14,000	Floating rate based on 3M EURIBOR	14,000	-	-
Portigon AG bonded loan*	11,390	Floating rate based on 3M EURIBOR	-	-	11,390
Total financial liabilities	**28,984**		**14,729**	**2,292**	**11,963**

* Key covenants refer to the Group's year-end debt/equity ratio and to the quarter-end net liquidity.

** At the end of 2013, the IKB Deutsche Industriebank loan is secured by a registered land charge without certificate amounting to EUR 5,581 thousand (end of 2012: EUR 5,581 thousand) on the production and development site in Meiningen.

*** Subsidized by the German Reconstruction Loan Company (Kreditanstalt für Wiederaufbau, KfW).

On June 17, 2013, the Company early repaid the EUR 14,000 thousand bonded loan with variable interest rates from IKB Deutsche Industriebank maturing in September 2013.

As part of a follow-on financing, ADVA Optical Networking SE entered into a EUR 25,000 thousand loan agreement with IKB Deutsche Industriebank in May 2013. The loan has a 5-year maturity and a fixed interest rate of 2.55% per annum. The loan principal will be repaid in 16 equal installments of EUR 1,563 thousand per quarter commencing in Q3 2014. In addition, a commission payment of EUR 100 thousand was due on the loan disbursement on June 13, 2013. The loan is valued according to the effective interest method.

The interest rate charged for interest-bearing financial liabilities during 2013 ranged between 2.45% and 2.75% p.a. on average.

The fair value of the financial liabilities is stated in note (26).

Capital management
The goal of ADVA Optical Networking's capital management is to provide sufficient funds to ensure ongoing operations and to support the Group's projected growth at any time. The Group defines capital as the total of stockholders' equity and financial liabilities. On December 31, 2013, stockholders' equity was at EUR 157,820 thousand or at 53.8% of the balance sheet total (prior year: EUR 153,909 thousand or 54.2% of the balance sheet total). Financial liabilities were at EUR 39,196 thousand on December 31, 2013 (prior year: EUR 28,984 thousand), with maturities typically exceeding the life of the assets being financed. The loan contracts require the compliance with specific key financial covenants. Financial covenants relate to the debt/equity-ratio and net liquidity per quarter-end. If financial covenants are not met, early redemption of financial liabilities may be requested. In 2013, ADVA Optical Networking complied to all financial covenants. In managing its capital, ADVA Optical Networking is focused on minimizing interest expenses, as long as access to funds is not at risk. Excess funds are used either to redeem debt, or they are invested in short-term interest-bearing term deposits or money market funds.

Cash pooling has been implemented for USD bank accounts. The respective cash balances are transferred to a pooling account on a daily basis. Interest is calculated based on the consolidated balances.

(14) Trade Accounts Payable and Other Current and Non-Current Liabilities

The trade accounts payable are non-interest-bearing and generally due within 30 to 90 days.

Other current liabilities on December 31 can be analyzed as follows:

(in thousands of EUR)	2013	2012
Liabilities due to employees		
for variable compensation and payroll	9,392	9,972
for vacation	854	1,084
related to option bonds and other share-based compensation instruments	89	388
Liabilities due to withheld wage income tax and social security contributions	1,510	1,527
Liabilities due to tax authorities	3,321	1,659
Obligations from subsidized research projects	2,609	2,845
Negative fair values of derivative financial instruments	519	41
Other	2,278	1,742
	20,572	**19,258**

On December 31, 2013, other non-current liabilities primarily include deferred rental expense of EUR 1,130 thousand (prior year: EUR 1,415 thousand) and obligations to complete subsidized research projects of EUR 1,026 thousand (prior year: EUR 1,540 thousand).

(15) Provisions

The table below lists changes in the composition of the Group's provisions in the reporting period:

(in thousands of EUR)	Jan. 1, 2013	Usage	Release	Appropriation	Transfer	Currency translation difference	Dec. 31, 2013
Current provisions							
Warranty provision	645	-287	-	1,045	-	-5	1,398
Personnel provisions	586	-365	-5	2,081	-	-114	2,183
Other short-term provisions	4,061	-3,365	-137	4,194	-	-89	4,664
	5,293	**-4,017**	**-142**	**7,320**	**-**	**-209**	**8,245**
Non-current provisions							
Personnel provisions	454	-	-2	216	-	-3	665
Other long-term provisions	285	-162	-	708	-	-89	742
	739	**-162**	**-2**	**924**	**-**	**-92**	**1,407**
	6,032	**-4,179**	**-144**	**8,244**	**-**	**-301**	**9,652**

The estimated expenses related to warranty claims reflect both past experience and current developments and are based on a percentage of sales revenues. Any differences between actual amounts and anticipated amounts are treated as changes in accounting estimates and affect earnings in the period in which the change occurs. Moreover, appropriations for specific risks of EUR 954 thousand were made in 2013.

Current personnel provisions mainly include expenses for severance payments as well as employee's accident insurance and other expenses resulting from legal requirements.

Other current provisions primarily include provisions for outstanding invoices of uncertain amount and timing and provisions for potential obligations from existing contracts.

Non-current personnel provisions mainly include liabilities from share-based compensation transactions.

On December 31, 2013, other non-current provisions mainly include provisions for onerous contracts. It is expected that this provision will be used between 2015 and 2016.

(16) Deferred Revenues

Deferred revenues include deferred service revenues, where the contracted services are recognized as revenues over the duration of the respective contracts. Some of the service revenues have a contractual maintenance period of up to 110 months and therefore incorporate a long-term element.

Deferred revenues also include revenues from product sales that have not been recognized because one or more of the recognition criteria has not been met.

(17) Stockholders' Equity

Capital transactions
In connection with the exercise of stock options, 200,175 shares were issued to employees of the Company and its affiliates out of conditional capital in 2013 (in 2012 in connection with the exercise of stock options 297,777 shares). The par value of EUR 200 thousand (prior year: EUR 298 thousand) was appropriated to share capital, whereas the premium resulting from the exercise of stock options as well as the exercise of option bonds in prior periods of EUR 175 thousand (prior year: EUR 336 thousand) was recognized within capital reserve.

In 2013, the revocation of an option bonds program resulted in the reclassification of EUR 597 thousand from capital reserve to long-term provisions, representing the fair value of outstanding option bonds at the date of the revocation.

Other information on the share option programs is included in note (31).

Common stock and share capital
ADVA Optical Networking SE had 48,022,827 no par value bearer shares (hereinafter "common shares") in issue on December 31, 2013 (prior year: 47,822,652).

The common shares entitle the holder to vote at the Annual Shareholders' Meeting and to receive dividends in case of a distribution. No restrictions are attached to the common shares.

Authorized capital
The existing authorized capital I has been completely canceled during the Annual Shareholders' Meeting on June 4, 2013, and replaced by a new authorized capital 2013/I. According to the Company's articles of association, the Management Board is authorized, subject to the consent of the Supervisory Board, to increase subscribed capital until June 3, 2018, only once or in successive tranches by a maximum of EUR 23,911 thousand by issuing new common shares in return for cash or non-cash contributions. Subject to the consent of the Supervisory Board, the Management Board is further authorized to decide whether to exclude stockholders' subscription rights. Stockholders' subscription rights can be excluded for capital increases for cash contributions as well as contributions in kind if during the term of this authorization and in exclusion of shareholder subscription rights, the shares issued against contributions in cash or in kind do not exceed 20% of the share capital.

Moreover, authorized capital III for the exercise of outstanding option bonds has been completely canceled during the Annual Shareholders' Meeting on June 4, 2013.

Conditional capital
The Annual Shareholders' Meeting on June 4, 2013, resolved to decrease the conditional capital 2003/2008 by EUR 297 thousand to EUR 2,229 thousand. In addition, the conditional capital 2011/I has been increased by EUR 625 thousand to EUR 2,553 thousand. The resolutions were registered in the commercial register on July 3, 2013.

Considering the above described capital transactions, the total conditional capital on December 31, 2013, amounts to EUR 4,582 thousand.

The changes in share capital, authorized and conditional capital are summarized below:

(in thousands of EUR)	Share capital	Authorized capital I	Authorized capital 2013/I	Authorized capital III	Conditional capital 2003 / 2008	Conditional capital 2011 / I
Jan. 1, 2013	**47,823**	**20,948**	**-**	**1,364**	**2,526**	**1,928**
Changes due to Annual Shareholders' Meeting resolutions	-	-20,948	23,911	-1,364	-297	625
Stock options exercised	200	-	-	-	-200	-
Dec. 31, 2013	**48,023**	**-**	**23,911**	**-**	**2,029**	**2,553**

Capital reserve
The capital reserve includes premium payments from the issuance of shares, as well as additional contributions to the Company's equity associated with the exercise of stock options and option bonds. Additionally, the capital reserve contains the correspondent accumulated compensation expenses from stock option programs amounting to EUR 14,605 thousand (prior year: EUR 14,450 thousand).

Accumulated other comprehensive loss
Accumulated other comprehensive loss is used to record exchange differences arising from the translation of the financial statements of foreign operations.

Changes in stockholders' equity are summarized in the consolidated statement of changes in stockholders' equity.

Voting Rights

According to section 21 paragraph 1 and section 26 of the German Securities Trading Law (Wertpapier-Handelsgesetz, WpHG) the Company published the following information on the ADVA Optical Networking homepage in 2013:

Date of change in investment	Name of investment owner	Threshold limit	Share of voting rights
Nov. 22, 2013	ING Investment Management Belgium S.A., Brussels, Belgium; ING Fund Management B.V, Den Haag, Netherlands; ING Investment Management Luxembourg S.A., Luxemburg, Luxemburg	below 3%	2.98%
Oct. 24, 2013	ING Investment Management Belgium S.A., Brussels, Belgium; ING Fund Management B.V, Den Haag, Netherlands; ING Investment Management Luxembourg S.A., Luxemburg, Luxemburg	above 3%	3.08%
Oct. 16, 2013	ING Investment Management Belgium S.A., Brussels, Belgium; ING Fund Management B.V, Den Haag, Netherlands; ING Investment Management Luxembourg S.A., Luxemburg, Luxemburg	below 3%	2.97%
Oct. 10, 2013	ING Investment Management Belgium S.A., Brussels, Belgium; ING Fund Management B.V, Den Haag, Netherlands; ING Investment Management Luxembourg S.A., Luxemburg, Luxemburg	above 3%	3.01%
Oct. 8, 2013	ING Investment Management Belgium S.A., Brussels, Belgium; ING Fund Management B.V, Den Haag, Netherlands; ING Investment Management Luxembourg S.A., Luxemburg, Luxemburg	below 3%	2.97%
Aug. 30, 2013	FMR LLC, Boston, USA	above 3%	3.02%
Aug. 13, 2013	ING Investment Management Belgium S.A., Brussels, Belgium; ING Fund Management B.V, Den Haag, Netherlands; ING Investment Management Luxembourg S.A., Luxemburg, Luxemburg	above 3%	3.06%
Jul. 11, 2013	ING Investment Management Belgium S.A., Brussels, Belgium; ING Fund Management B.V, Den Haag, Netherlands; ING Investment Management Luxembourg S.A., Luxemburg, Luxemburg	below 3%	2.99%
Jun. 10, 2013	Norwegian Ministry of Finance/Norges Bank, (the Central Bank of Norway), Oslo, Norway	above 3%	3.01%
May 3, 2013	ING Investment Management Belgium S.A., Brussels, Belgium; ING Fund Management B.V, Den Haag, Netherlands; ING Investment Management Luxembourg S.A., Luxemburg, Luxemburg	above 3%	3.002%

Notes to the Consolidated Income Statement

(18) Revenues

IIn 2013 and 2012, revenues included EUR 40,231 thousand and EUR 37,921 thousand for services, respectively. The remaining revenues relate mainly to product sales.

A segmentation of revenues by geographic region is provided in the section on segment reporting under note (25).

(19) Other Operating Income and Expenses

(in thousands of EUR)	2013	2012
Other operating income		
Government grants received	1,686	1,289
Reimbursement for joint development by a strategic partner	410	-
Release of bad debt allowances	474	261
Release of provisions	144	293
Other	406	443
	3,120	**2,286**
Other operating expenses		
Impairments on trade accounts receivable	-193	-8
Other	-396	-219
	-589	**-227**
Other operating income and expenses, net	**2,531**	**2,059**

(20) Interest Income and Expenses

Interest income primarily includes interest from daily bank deposits and from other short-term deposits with maturities between one day and three months.

Interest expenses are primarily incurred on financial liabilities and on the sale of receivables. Refer to notes (13) and (8) for further details.

(21) Other Financial Gains and Losses, net, and Derivative Financial Instruments

Other financial gains and losses, net, comprise the following:

(in thousands of EUR)	2013	2012
Foreign currency exchange gains	4,782	9,150
thereof: gains from forward rate agreements	*255*	*486*
Foreign currency exchange losses	-6,257	-8,316
thereof: losses from forward rate agreements	*-1,069*	*-309*
	-1,475	**834**

Forward rate agreements
The Group entered into nine forward rate agreements to hedge foreign currency exposure of expected future cash flows between August 8, 2013, and December 13, 2013. These agreements mature between March 28, 2014 and December 30, 2014. In 2013, unrealized profits and losses, net, amounted to negative EUR 519 thousand.

Between October 17, 2012 and June 12, 2013, the Group entered into six forward rate agreements that matured in 2013. A net result of negative EUR 295 thousand was realized on these transactions.

Fair value disclosures
On December 31, the Group held the following financial instruments measured at fair value:

(in thousands of EUR)	Fair value		Nominal value	
	2013	2012	2013	2012
Forward rate agreements	-519	7	34,624	14,366

The nominal value is the accounting value from which payments are derived (underlying transaction). Since the nominal value itself is not at risk, it is the potential for changes in foreign exchange rates, interest rates and prices that is hedged.

The fair value reflects the credit risk of the instrument. Since the Group only uses standard instruments for its hedges, the fair value is determined using market prices and is not netted against any contrary trend in the value of underlying transactions.

The fair value of these transactions is presented within other current assets and other current liabilities in the statement of financial position.

(22) Income Taxes

Income taxes in Germany consist of corporate income tax, the solidarity surcharge and trade taxes. The tax calculation in foreign countries is based on the applicable local tax rates. They vary between 13% and 38% (prior year: between 16.5% and 38.0%).

The table below shows the components of the Group's total income tax expenses:

(in thousands of EUR)	2013	2012
Current taxes		
Current income tax charge	-794	-2,121
Adjustments in respect of current income tax for prior years	3,082	132
	2,288	**-1,989**
Deferred taxes		
Temporary differences and loss carry-forwards	-1,123	134
Changes in tax rates	-14	72
	-1,137	**206**
Income tax (expense) benefit, net	**1,151**	**-1,783**

A reconciliation of income taxes based on the accounting profit and the expected domestic income tax rate for the parent company of 27.73% (prior year: 27.73%) to effective income tax (expense) benefit, net, is presented below.

(in thousands of EUR)	2013	2012
Accounting profit before tax	**4,356**	**18,505**
Expected statutory tax expense	**-1,208**	**-5,131**
Tax rate adjustments	-14	-72
Tax for prior periods	3,082	132
Foreign tax rate differential	-229	-58
Non-tax-deductible stock option expenses	-68	-130
Differences from foreign branch offices	42	-73
Other non-tax-deductible expenses	-363	-108
Adjustments to recognition of deferred tax assets	-2,622	3,667
Utilization of loss carry-forwards not recognized before	2,495	-
Not capitalized deferred tax assets for tax losses	58	-
Other differences	-22	-10
Income tax benefit (expense), net	**1,151**	**-1,783**
Effective tax rate	**-26.4%**	**9.6%**

Income from current taxes for prior periods results mainly from the release of prior years' tax provisions due to an appeal decision for the tax audit for 2001-2004. The net income effect from adjustment of deferred tax assets is related to the increase of deferred tax assets for tax losses in ADVA Optical Networking SE by EUR 2,488 thousand for recognition before 2012 (prior year: nil).

In 2013, the tax authorities in Munich announced a tax audit for fiscal years 2007 to 2010 to ADVA Optical Networking SE.

The deferred tax assets and deferred tax liabilities on December 31, 2013 and 2012 relate to the following:

	2013		2012	
(in thousands of EUR)	Deferred tax assets	Deferred tax liabilities	Deferred tax assets	Deferred tax liabilities
Current assets				
Trade accounts receivable	87	-7	25	-10
Inventories	1,660	-658	1,877	-305
Other current assets	98	-	85	-14
Total current assets	**1,845**	**-665**	**1,987**	**-329**
Non-current assets				
Property, plant and equipment	240	-750	345	-1,012
Capitalized development projects	-	-14,276	-	-12,692
Purchased technology	38	-	100	-
Other intangible assets	14	-2,528	51	-3
Other non-current assets	414	-	598	-
Total non-current assets	**706**	**-17,554**	**1,094**	**-13,707**
Current liabilities				
Trade accounts payable	12	-3	33	-111
Provisions	1,016	-	1,234	-
Deferred revenues	932	-13	942	-22
Other current liabilities	295	-	75	-
Total current liabilities	**2,255**	**-16**	**2,284**	**-133**

(in thousands of EUR)	2013 Deferred tax assets	2013 Deferred tax liabilities	2012 Deferred tax assets	2012 Deferred tax liabilities
Non-current liabilities				
Financial liabilities	2	-	7	-
Other non-current liabilities	1,364	-70	1,300	-
Total non-current liabilities	**1,366**	**-70**	**1,307**	**-**
Loss carry-forwards				
German tax loss carry-forward	3,956	-	-	-
thereof: current	*791*	-	-	-
thereof: non-current	*3,165*	-	-	-
Foreign tax loss carry-forward	4,869	-	5,819	-
thereof: current	*1,177*	-	*840*	-
thereof: non-current	*3,692*	-	*4,979*	-
Total loss carry-forwards	**8,825**	**-**	**5,819**	**-**
Deferred tax assets (liabilities)	**6,172**	**-18,304**	**12,491**	**-14,169**
thereof: current	*6,068*	*-680*	*5,111*	*-462*
thereof: non-current	*8,929*	*-17,624*	*7,380*	*-13,707*

Temporary differences are differences between the carrying amount of an asset or liability in the balance sheet according to IFRS and its tax base.

Deferred tax assets have been recognized for German and foreign tax loss carry-forwards since the Group determined a positive tax forecast due to projected positive market developments in the Optical+Ethernet transport solution market and the leading market position of ADVA Optical Networking in the regional markets, which are relevant for the assessment of loss carry-forwards as reported.

The German and foreign tax loss carry-forwards on December 31 comprise:

(in thousands of EUR)	2013	2012
ADVA Optical Networking SE, Meiningen, Germany	119,265	123,061
ADVA Optical Networking AS, Oslo, Norway	3,572	3,494
ADVA Optical Networking North America, Inc., Norcross/Atlanta (Georgia), USA	111,935	118,942
ADVA Optical Networking Ltd., York, United Kingdom	5,279	4,905
ADVA Optical Networking LLC., Riyadh, Kingdom of Saudi Arabia	46	55
ADVA Optical Networking Serviços Ltda., São Paulo, Brazil	-	8
	240,097	**250,465**

In 2013, the tax authorities released a decision to appeals related to the finalized tax audit for 2001-2004 in favor of ADVA Optical Networking SE and amended respective tax assessments. The effects are included in the tax loss carry-forwards and respective notes hereto. Deferred tax assets have been recognized in respect of tax losses in the amount of EUR 14,265 thousand (prior year: nil) due to a reasonable assurance that taxable profits will be recognized in the near future that can be offset against loss carry-forwards.

Tax losses of ADVA Optical Networking North America decreased based on the tax return 2012 regarding the prior year-end. The company has not reported further tax losses over an aggregated three-year-period and taking into account the following considerations there is a reasonable assurance that taxable profits will be recognized in the near future that can be offset against loss carry-forwards.

Pursuant to the U.S. Tax Act, federal tax loss carry-forwards in the U.S. expire after twenty years. Further, the utilization of a portion of loss carry-forwards is subject to annual limitations. Consequently, deferred tax assets have not been recognized in respect of loss carry-forwards in ADVA Optical Networking North America in the amount of EUR 101,680 thousand (prior year: EUR 106,184 thousand).

Furthermore, deferred tax assets for loss carry-forwards for state and local purposes expire in between five and twenty years. The utilization of those tax loss carry-forwards for state and local purposes is also subject to annual limitations. Consequently, deferred tax assets in the amount of EUR 2,983 thousand (prior year: EUR 3,164 thousand) have not been recognized in ADVA Optical Networking North America in respect of tax losses for state and local purposes.

Deferred tax assets on loss carry-forwards and temporary differences in ADVA Optical Networking Oslo and ADVA Optical Networking Riyadh have not been recognized. The companies have a history of losses, and the recognition of taxable profits that could be offset against loss carry-forwards is not certain in the near future. In addition, these loss carry-forwards may not be used to offset against future taxable profits elsewhere in the Group.

Whether or not deferred tax assets are realized depends on the generation of future taxable income during periods in which these temporary differences are deductible. The Group has considered the scheduled reversal of deferred tax liabilities and projected future taxable income in making this assessment.

On December 31, 2013 and 2012, no deferred tax liabilities on retained earnings of group companies have been recognized. ADVA Optical Networking committed that there will be no distribution of currently undistributed earnings from the Company's major subsidiaries in the near future. The amount of temporary differences for which no deferred tax liabilities have been recognized totals EUR 303 thousand (prior year: EUR 334 thousand).

Tax assets of EUR 379 thousand (prior year: EUR 136 thousand) include primarily corporate tax refunds for current year in the amount of EUR 354 thousand (prior year: EUR 118 thousand), as well as withholding tax and corporate tax refunds from prior periods of EUR 25 thousand (prior year: EUR 18 thousand).

Tax liabilities primarily include corporate income tax and trade tax liabilities.

Other Disclosures

(23) Notes to the Consolidated Cash Flow Statement

The consolidated cash flow statement has been prepared in accordance with IAS 7.

Cash and cash equivalents disclosed in the cash flow statement coincide with the position "cash and cash equivalents" presented in the statement of financial position.

Cash flows from investing and financing activities are determined directly, whereas the cash flow from operating activities is derived indirectly from the consolidated income before tax. When cash flow from operating activities is calculated, the changes in assets and liabilities are adjusted for the effects of currency translation. As a result, it is not possible to reconcile the figures to the differences in the published consolidated statement of financial position.

Cash and cash equivalents to which the Group only has restricted access are explained in note (7).

(24) Earnings per Share

In accordance with IAS 33, basic earnings per share are calculated by dividing consolidated net income by the weighted average number of shares outstanding.

In the period under review, there were no material effects that diluted earnings per share. Diluted earnings per share are calculated by adjusting the average number of shares outstanding by the number of potential shares arising from granted and exercisable stock options on the balance sheet date.

Regarding net income, no effects of dilution need to be considered in 2013 and 2012.

The following table reflects the number of shares used in the computation of basic and diluted earnings per share:

	2013	2012
Weighted average number of shares (basic)	**47,897,901**	**47,626,641**
Effect of dilution from stock options	688,297	1,155,534
Weighted average number of shares (diluted)	**48,586,198**	**48,782,175**

There have been no other material transactions involving ordinary shares or potential shares between the balance sheet date and the date of authorization for issue of these financial statements.

(25) Segment Reporting

In accordance with IFRS 8, operating segments are identified based on the way information is reported internally to the chief operating decision maker and regularly reviewed to make decisions about resources to be allocated to the segment and assess its performance. Within the ADVA Optical Networking Group, management decisions are based on pro forma operating income. Pro forma financial information excludes non-cash charges related to share-based compensation plans and amortization and impairment of goodwill and acquisition-related intangible assets. Income from capitalization of development expenses is shown as a separate line item and not deducted from research and development expenses.

Segment information on December 31, 2013 is analyzed as follows:

(in thousands of EUR)	Pro forma financial information	Intangible assets from acquisitions	Goodwill	Compensation expenses	Disclosure of R&D expenses	Consolidated financial information
Revenues	310,702	-	-	-	-	310,702
Cost of goods sold	-188,561	-641	-	-90	-	-189,292
Gross profit	**122,141**	**-641**	**-**	**-90**	**-**	**121,410**
Gross margin	***39.3%***					***39.1%***
Selling and marketing expenses	-46,717	-42	-	-355	-	-47,114
General and administrative expenses	-26,225	-	-	-124	-	-26,349
Research and development expenses	-65,649	-	-	-344	22,490	-43,503
Income from capitalization of development expenses	22,490	-	-	-	-22,490	-
Other operating income	3,120	-	-	-	-	3,120
Other operating expenses	-589	-	-	-	-	-589
Operating income	**8,571**	**-683**	**-**	**-913**	**-**	**6,975**
Operating margin	***2.8%***					***2.2%***
Segment assets	**272,149**	**1,054**	**19,875**	**-**	**-**	**293,078**

Segment information on December 31, 2012 is analyzed as follows:

(in thousands of EUR)	**Pro forma financial information**	**Intangible assets from acquisitions**	**Goodwill**	**Compensation expenses**	**Disclosure of R&D expenses**	**Consolidated financial information**
Revenues	330,069	-	-	-	-	330,069
Cost of goods sold	-196,820	-1,506	-	-138	-	-198,464
Gross profit	**133,249**	**-1,506**	**-**	**-138**	**-**	**131,605**
Gross margin	*40.4%*					*39.9%*
Selling and marketing expenses	-46,259	-114	-	-430	-	-46,803
General and administrative expenses	-25,725	-	-	-260	-	-25,985
Research and development expenses	-65,055	-	-	-516	23,529	-42,042
Income from capitalization of development expenses	23,529	-	-	-	-23,529	-
Other operating income	2,286	-	-	-	-	2,286
Other operating expenses	-227	-	-	-	-	-227
Operating income	**21,798**	**-1,620**	**-**	**-1,344**	**-**	**18,834**
Operating margin	***6.6%***					***5.7%***
Segment assets	**262,949**	**1,270**	**19,876**	**-**	**-**	**284,095**

Additional information by geographical regions:

(in thousands of EUR)	2013	2012
Revenues		
Germany	71,320	77,633
Rest of Europe, Middle East and Africa	133,842	121,631
Americas	88,325	112,647
Asia-Pacific	17,215	18,158
	310,702	**330,069**

(in thousands of EUR)	Dec. 31, 2013	Dec. 31, 2012
Non-current assets		
Germany	72,733	67,548
Rest of Europe, Middle East and Africa	11,848	13,454
Americas	9,996	10,864
Asia-Pacific	1,959	2,431
	96,536	**94,297**
Deferred tax assets		
Germany	4,137	113
Rest of Europe, Middle East and Africa	1,526	1,544
Americas	9,153	10,670
Asia-Pacific	181	164
	14,997	**12,491**

Revenue information is based on the shipment location of the customers.

In 2013, the share of revenues allocated to major customers was EUR 119,227 thousand (prior year: EUR 110,935 thousand). In both reporting periods, revenues with two major customers exceeded 10% of total revenues.

Non-current assets and deferred tax assets are attributed based on the location of the respective Group company. Non-current assets for segment reporting consist of property, plant and equipment, intangible assets and finance lease equipment.

(26) Additional Disclosures on Financial Instruments

The following tables analyze carrying amounts, amortized costs and fair values according to valuation categories. Only assets and liabilities, which fall into the categories defined by IFRS 7, are shown, so that the total amounts disclosed do not correspond to the balance sheet totals of each year.

(in thousands of EUR, on Dec. 31, 2013)	Valuation category in accordance with IAS 39*	Carrying amount	Amounts recognized according to IAS 39 Amortized cost	Amounts recognized according to IAS 39 Fair value recognized in profit and loss	Fair value
Assets					
Cash and cash equivalents	LaR	80,934	80,934	-	80,934
Trade accounts receivable	LaR	52,739	52,739	-	52,739
Loans to associates and joint ventures	LaR	229	229	-	229
Total active financial instruments		**133,902**	**133,902**	**-**	**133,902**
Liabilities					
Financial liabilities (current and non-current)	FLAC	39,196	39,196	-	38,472
Trade accounts payable	FLAC	26,515	26,515	-	26,515
Other liabilities (current and non-current)	FLAC	12,263	12,263	-	12,263
Other current liabilities (derivatives without a hedging relationship)	FVTPL	519	-	519	519
Total passive financial instruments		**78,493**	**77,974**	**519**	**77,769**
Of which aggregated by category in accordance with IAS 39:					
Loans and receivables (LaR)		133,902	133,902	-	133,902
Financial liabilities at fair value through profit or loss (FVTPL)		519	-	519	519
Financial liabilities at amortized cost (FLAC)		77,974	77,974	-	77,250

* Abbreviations used for the IAS 39 categories:
- LaR: Loans and receivables
- FVTPL: Financial assets and liabilities at fair value through profit or loss
- FLAC: Financial liabilities at amortized cost

(in thousands of EUR, on Dec. 31, 2012)	Valuation category in accordance with IAS 39*	Carrying amount	Amounts recognized according to IAS 39: Amortized cost	Amounts recognized according to IAS 39: Fair value recognized in profit and loss	Fair value
Assets					
Cash and cash equivalents	LaR	70,625	70,625	-	70,625
Trade accounts receivable	LaR	55,464	55,464	-	55,464
Other current assets (derivatives without a hedging relationship)	FVTPL	48	-	48	48
Total active financial instruments		**126,137**	**126,089**	**48**	**126,137**
Liabilities					
Financial liabilities (current and non-current)	FLAC	28,984	28,984	-	29,394
Trade accounts payable	FLAC	38,078	38,078	-	38,078
Other liabilities (current and non-current)	FLAC	13,246	13,246	-	13,246
Other current liabilities (derivatives without a hedging relationship)	FVTPL	41	-	41	41
Total passive financial instruments		**80,349**	**80,308**	**41**	**80,759**
Of which aggregated by category in accordance with IAS 39:					
Loans and receivables (LaR)		126,089	126,089	-	126,089
Financial assets at fair value through profit or loss (FVTPL)		48	-	48	48
Financial liabilities at fair value through profit or loss (FVTPL)		41	-	41	41
Financial liabilities at amortized cost (FLAC)		80,308	80,308	-	80,718

The fair value of financial liabilities has been calculated based on future cash flows by using arm's length interest rates. On December 31, 2013 and 2012, respectively, no financial instruments were measured at cost or at fair value through other comprehensive income.

The Group uses the following hierarchy for determining the fair value of financial instruments:

Level 1: Quoted prices in active markets for identical assets or liabilities.

Level 2: Techniques for which all inputs that have a significant effect on the recorded fair value are observable, either directly or indirectly. Forward rate agreements are measured using quoted forward exchange rates and yield curves derived from quoted interest rates according to the maturities of the contract.

Level 3: Techniques, which use inputs that are not based on observable market data.

Fair values of assets and liabilities at fair value through profit or loss are calculated using level 2 valuation techniques. On December 31, 2013, no valuations were made according to levels 1 or 3. In 2013 and 2012, no transfers between hierarchy levels occurred.

The Group has not used the option to designate financial assets as "at fair value through profit or loss" on initial recognition of those assets. The Group has neither used the option to designate financial liabilities as "at fair value through profit or loss" on initial recognition of those liabilities.

Gains and losses as well as interest income and expenses from financial instruments are analyzed in the table below:

(in thousands of EUR)	Note	2013	2012
Gains and losses			
Financial assets at fair value through profit or loss	(21)	-814	177
Loans and receivables	(8, 19)	-276	-1,869
Interest income and expenses			
Cash and cash equivalents	(20)	96	133
Financial liabilities measured at amortized cost	(13)	-929	-1,016

(27) Financial Risk Management

Due to ADVA Optical Networking's business activities financial risks arise in essence from loss in value of inventories, fluctuations in international currencies, payment term extension and payment delay of customers as well as failure to discharge payment obligations and changes in interest rate levels. The positions with respect to those risks are analyzed below. Goals, guidelines and processes of the Group's risk management system are discussed in detail in the risk report within the Management Report. ADVA Optical Networking's capital management is described in note (13).

Global risk management is carried out by a central treasury department under policies approved by the Management Board.

Inventory risk
Technological obsolescence, as well as short-term changes in customer demand and manufacturing processes may trigger significant inventory depreciation. Preventive measures to minimize inventory depreciation include an integrated sales and operations planning process and monthly reviews of inventory depreciation requirements on item level. In 2013, inventory depreciation amounted to EUR 2,211 thousand after EUR 4,466 thousand in 2012.

Foreign currency risk
Foreign currency risks arise from unfavorable changes in foreign currency exchange rates and according to IFRS affect monetary financial instruments denominated in currencies other than the functional currency of the respective Group entity.

Due to a major portion of the Group's revenues and costs being generated in foreign currencies, the Group is particularly subject to fluctuations of the EUR against the USD and GBP as well as USD against GBP.

Sensitivity analysis
The following table summarizes the foreign currency exposure on the net monetary positions and illustrates the effect on 2013 profit or loss of a 10% change in the EUR/USD, EUR/GBP and USD/GBP rates:

(in thousands of EUR)	EUR/USD	EUR/GBP	USD/GBP
ADVA Optical Networking SE	2,792	673	-
ADVA Optical Networking York	-	1,018	3,302
ADVA Optical Networking North America	5,758	-	-16
ADVA Optical Networking Trading	173	-	-
Net exposure in consolidated financial statements	**8,722**	**1,691**	**3,286**
Appreciation of USD vs. EUR and of GPB vs. EUR and USD	10.0%	10.0%	10.0%
Total effect on net income	**872**	**169**	**329**

A depreciation of the currencies of 10% would have an equal and opposite effect.

In addition, a weakening of foreign currencies, especially of the USD and the GBP, can have a significant financial impact on the ability to price ADVA Optical Networking's products competitively.

Customer payment terms risk
In ADVA Optical Networking's competitive Optical+Ethernet connectivity market, customers may request to extend payment terms. The extension of the Group's weighted-average payment terms would have a negative impact on working capital and cash levels. In order to mitigate this risk, there is a three-step process in place governing the escalation of payment terms extension requests. In addition, at the end of 2013, the Group had frame contracts in place to sell receivables from two customers (at the end of 2012: from two customers) to financial institutions.

Customer On-Time Payment Risk
If customers pay their open invoices at a later point in time than contractually agreed, there is an adverse impact on working capital and cash levels. In addition, once receivables become overdue, the likelihood of payment default increases. Credit risks are accounted for as depreciation or impairment of individual assets. In 2013, depreciation on trade accounts receivable due to doubtful accounts amounted to EUR 557 thousand (2012: EUR 2,122 thousand). The maximum risk of loss is the carrying value of trade accounts receivable of EUR 52,739 thousand (prior year: EUR 55,464 thousand). In order to mitigate the on-time payment risk, the root causes for a customer not paying in time are addressed in close collaboration between the Group's Finance and Sales organizations. Underlying product, service and billing issues are addressed, and in cases where there are no such issues or where such issues have been resolved successfully and open invoices are still not paid, customer credit limits are adjusted, customer shipments are stopped and/or customer prepayment will be required for future transactions.

Liquidity risk
The Group is exposed to liquidity risk, which is the risk that the Group will not be able to meet its obligations as they fall due. The Group manages this risk by forecasting its cash and working capital requirements. The Management Board of ADVA Optical Networking does not consider this uncertainty to be likely or to have a major impact on the Group.

Interest rate risk
ADVA Optical Networking is exposed to interest rate risks because group entities invest funds at fixed and floating interest rates. On the balance sheet date, financial liabilities arise only in the parent company. One bonded loan with a nominal value of EUR 11,500 thousand carries variable interest. All other financial liabilities carry fixed interest rates. Based on the currently low interest rates on the EUR money market and the uncertain macro-economic environment for the EUR zone, the Group's risk resulting from changes in interest rates at current is not material.

The table below analyzes the Group’s non-derivative financial liabilities into relevant maturity groupings based on the remaining time at the balance sheet date to the contractual maturity date:

			Future cash flows					
			≤ 12 months		13 – 36 months		> 36 months	
(in thousands of EUR, on Dec. 31, 2013)	Note	Carrying value	Redemption	Interest	Redemption	Interest	Redemption	Interest
Financial liabilities	(13)	39,196	4,199	986	14,211	1,465	20,786	283
Finance leases	(12)	14	5	1	9	-	-	-
Trade accounts payable and other current and non-current liabilities	(14)	49,243	47,087	-	1,707	-	449	-
		88,453	**51,291**	**987**	**15,927**	**1,465**	**21,235**	**283**

			Future cash flows					
			≤ 12 months		13 – 36 months		> 36 months	
(in thousands of EUR, on Dec. 31, 2012)	Note	Carrying value	Redemption	Interest	Redemption	Interest	Redemption	Interest
Financial liabilities	(13)	28,984	14,729	697	2,292	746	11,963	330
Finance leases	(12)	41	27	2	14	1	-	-
Trade accounts payable and other current and non-current liabilities	(14)	60,291	57,336	-	2,249	-	706	-
		89,316	**72,092**	**699**	**4,555**	**747**	**12,669**	**330**

(28) Other Financial Obligations and Financial Commitments

Lease commitments
The Group has non-cancellable operating leases, primarily for buildings and cars. There are no sub-lease agreements.

The future minimum lease payments due on operating leases are listed in the table below:

(in thousands of EUR)	Dec. 31, 2013	Dec. 31, 2012
Up to one year	4,492	4,404
One to five years	13,649	13,317
More than five years	934	2,445
	19,075	**20,166**

Lease payments for buildings including parking spaces amount to EUR 4,645 thousand and EUR 3,720 thousand in 2013 and 2012, respectively. Lease payments for cars consisting of monthly installments plus servicing charges and road tax totaled EUR 1,267 thousand and EUR 1,119 thousand in 2013 and 2012, respectively.

Other obligations
On December 31, 2013, the Group had purchase commitments totaling EUR 3,793 thousand (on December 31, 2012: EUR 6,173 thousand) in respect to suppliers.

Guarantees
Group entities have issued guarantees in favor of customers. On December 31, 2013, performance bonds with a maximum guaranteed amount of EUR 374 thousand were issued. Further, the parent company granted an irrevocable guarantee of up to GBP 1,500 thousand for liabilities of ADVA Optical Networking York and up to EUR 500 thousand for liabilities of ADVA Optical Networking Bangalore as well as a rental guarantee for ADVA Optical Networking Oslo up to a maximum amount equal to six months rental plus utility payments.

(29) Contingent Liabilities

In the normal course of business, claims may be asserted or lawsuits filed against the Company and its subsidiaries from time to time. On December 31, 2013, ADVA Optical Networking does not expect that potential titles or litigations in detail or in total will have a material impact on its financial position or operating performance.

(30) Auditor's Fees

In 2013 and 2012, the following fees charged by the legal auditor were agreed and recognized as expenses:

(in thousands of EUR)	2013	2012
Year-end audit	273	271
Other consulting services	2	27
	275	**298**

(31) Stock Option Programs

To date, the Company has issued stock options (Plan IX and Plan XIV) and stock appreciation rights for employees (Plan XI, Plan XIII, Plan XV and Plan XVI). On December 31, 2013, three share-based compensation programs for the Management Board and employees of the Company and its subsidiaries were still in existence.

On October 1, 2008, stock options from Plan IX and stock appreciation rights from Plan XI were offered to be exchanged for new rights. All rights of those plans issued before January 1, 2008, were allowed for exchange on the due date, whereby three old rights were exchanged for two new rights of the respective option program. The calculation of the strike price and vesting period of the new options and stock appreciation rights is based on the latest contracts. The new options and stock appreciation rights are listed as Plan IXa and Plan XIa in this report.

In December 2010, the Supervisory Board approved a profit limitation for all options granted to members of the Management Board out of Plan IX. The options issued with those changed conditions are referred to as Plan IXb.

In February 2011, the Management Board set up a stock appreciation rights program. These stock appreciation rights can be exercised until December 31, 2015. 50% of the option rights may not be exercised until 2012 and the remaining 50% until 2013. The agreements include a profit limit of EUR 20.00 per option. The new program is referred to as Plan XIII. Respective option rights were granted on March 1, 2011. There will be no further issuance of stock appreciation rights from Plan XIII.

In August 2011, the Management Board set up two new programs for the issuance of option rights and stock appreciation rights. Both contracts stipulate a four-year vesting period and a total contractual life of seven years for the respective rights issue. The rights may only be exercised if the volume weighted average of the Company share closing prices on the ten stock exchange trading days before the first day of each exercise period in which the option is exercised is at least 120% of the purchase price. In addition, the calculation of the maximum bonus for stock appreciation rights is based on the share price at the date of exercise, with the share price being capped at EUR 20.00. Consecutively, the new program for issuance of option rights is referred to as Plan XIV and the program for issuance of stock appreciation rights is referred to as Plan XV.

In August and November 2013, new options for employees as well as the Management Board were issued from Plan XIV. The options issued for the Management Board include a profit limitation for all options granted and are referred to as Plan XIVa.

Due to legal reasons, the existing option bonds program (Plan X) has been revoked in 2013. All outstanding option bonds from this plan have been either exchanged into stock appreciation rights or settled in cash. A new stock appreciation rights plan (Plan XVI) has been established that includes contractual terms corresponding to Plan X. All stock appreciation rights from Plan XVI have already vested. No further benefits have been granted in the course of the exchange. Additional information on the exchange is included in note (17).

All option rights are non-transferable. They may only be exercised as long as the entitled person is employed on a permanent contract by the Company or by a company in which ADVA Optical Networking SE has direct or indirect interest. Option rights issued to apprentices may only be exercised if the apprentices are hired by the Company or by an affiliated company on a permanent contract. All option rights expire upon termination of the employment contract. In the event that the person entitled dies, becomes unable to work or retires, special provisions come into force.

The group of people to whom option rights can be issued is defined separately for each stock option program. According to the resolution on June 4, 2013, 19.58% of option rights authorized pursuant to Plan XIV can be issued to members of the Management Board, 2.63% to the management of affiliated companies, 31.31% to Company employees, and 46.48% to employees of affiliated companies. The Management Board specifies the exact group of people entitled to exercise rights and the scope of each offer.

Subject to the conditions under which option rights are issued, each option right entitles the individual to purchase one common share in the Company. The stock appreciation rights entitle the recipient to receive a bonus in the amount of the difference between the defined strike price and the stock market price on the date of exercise (cash settlement). The Company may opt to replace the granted stock appreciation rights with other participation rights as long as such other participation right economically equals the replaced stock appreciation right. The conditions of issue specify the term, the exercise price (strike price), any qualifying periods and the defined exercise periods.

Apart from those rights referred to as Plan XIII all option rights can be exercised over a total period of seven years. One-third of the option rights granted pursuant to Plan IX and XI may not be exercised until two years after the grant date, another one-third three years after the grant date and the final one-third four years after the grant date. 50% of the option rights granted pursuant to Plan X may not be exercised until two years after the grant date and the remaining 50% three years after the grant date. The new option plans XIV und XV comprise a uniform vesting period of four years for all options and stock appreciation rights issued. The strike price equals the average stock price of the last ten trading days prior to the grant date. The minimum strike price is defined as the final auction price on the day when the option rights are issued. To exercise the options, certain exercise hurdles per tranche are to be considered. Exercise hurdles comprise a surplus on the strike price of 10%, 20% and 30% for the first, second and third tranche of Plan IX, and of 10% and 20% for the first and second tranche of Plan X. The exercise hurdle on Plan XIV comprises a surplus on the strike price of 20%.

Exercise periods are regularly linked to key business events in the Company's calendar and each have a defined term. Certain other business events can lead to blocking periods, during which option rights cannot be exercised. Insofar as regular exercise periods overlap with such blocking periods, the exercise deadline shall be extended by the corresponding number of exercise days immediately after the end of such a blocking period. Option rights may be exercised only on days on which commercial banks are open in Frankfurt am Main, Germany.

The fair value of stock options and stock appreciation rights is estimated by simulation (Monte Carlo method) using a program that was especially adjusted to the underlying plans and based on the assumed strategy for the exercise (earliest possible date). The following computation parameters apply for option rights issued in 2013 and stock appreciation rights re-valued on December 31, 2013:

	Plan XI	Plan XIa	Plan XIII	Plan XIV	Plan XIVa	Plan XV	Plan XVI
Weighted average share price (in EUR)	3.74	3.74	3.74	3.97	3.87	3.74	3.74
Average strike price (in EUR)	3.36	1.75	3.22	4.01	3.90	3.57	1.74
Expected volatility (in % per year)	41.36%	40.10%	40.10%	56.47%	53.52%	51.02%	36.82%
Term (in years)	7	7	4.9	7	7	7	7
Risk-free interest rate (in % per year)	0.37%	0.24%	0.24%	0.68%	0.65%	0.82%	0.19%

The volatility is specified as fluctuation of the share price compared to the average share price of the period. In each case, expected volatility is calculated based on historic share prices (historic volatility). The risk-free interest rate is based on information on risk-free investments with corresponding terms.

For the calculation of the fair value of options, ADVA Optical Networking assumed that no dividends will be paid to stockholders.

Changes in the number of option rights outstanding are detailed in the tables below.

Stock Option Program 2003 (Plan IX)

	Number of options	Weighted average strike price (in EUR)
Options outstanding on Jan. 1, 2012	**1,762,841**	**3.66**
Granted options	-	-
Exercised options	-130,123	1.95
Forfeited options	-38,567	3.99
Expired options	-9,000	6.98
Options outstanding on Dec. 31, 2012	**1,585,151**	**3.77**
Granted options	-	-
Exercised options	-102,833	2.00
Forfeited options	-248,535	4.60
Expired options	-157,500	7.65
Options outstanding on Dec. 31, 2013	**1,076,283**	**3.18**
Of which exercisable	948,359	3.13

The weighted average remaining contractual life for option rights outstanding on December 31, 2013, was 2.25 years. The strike price for those options is between EUR 1.00 and EUR 11.37.

Stock options exercised in 2013 had an average share price of EUR 3.97 on the exercise date.

Stock Option Program 2003 (Plan IXa)

All options from this plan have been issued in the course of the stock option exchange offer on October 1, 2008.

	Number of options	Weighted average strike price (in EUR)
Options outstanding on Jan. 1, 2012	**821,680**	**1.75**
Granted options	-	-
Exercised options	-167,654	1.75
Forfeited options	-20,314	1.75
Expired options	-	-
Options outstanding on Dec. 31, 2012	**633,712**	**1.75**
Granted options	-	-
Exercised options	-97,342	1.75
Forfeited options	-10,134	1.75
Expired options	-	-
Options outstanding on Dec. 31, 2013	**526,236**	**1.75**
Of which exercisable	526,236	1.75

The weighted average remaining contractual life for option rights outstanding on December 31, 2013, was 1.85 years. The strike price for those options is EUR 1.75.

Stock options exercised in 2013 had an average share price of EUR 3.89 on the exercise date.

Stock Option Program 2003 for the Management Board (Plan IXb)

	Number of options	Weighted average strike price (in EUR)
Options outstanding on Jan. 1, 2012	**245,000**	**3.31**
Granted options	-	-
Exercised options	-	-
Forfeited options	-	-
Expired options	-	-
Options outstanding on Dec. 31, 2012	**245,000**	**3.31**
Granted options	-	-
Exercised options	-	-
Forfeited options	-25,000	2.55
Expired options	-	-
Options outstanding on Dec. 31, 2013	**220,000**	**3.40**
Of which exercisable	146,666	3.40

The weighted average remaining contractual life for option rights outstanding on December 31, 2013, was 3.36 years. The strike price for those options is between EUR 2.55 and EUR 5.04.

Option Bonds for Employees 2005 (Plan X)

	Number of option bonds	Weighted average strike price (in EUR)
Option bonds outstanding on Jan. 1, 2012	**600,750**	**4.58**
Granted option bonds	-	-
Exercised option bonds	-	-
Forfeited option bonds	-54,500	1.50
Expired option bonds	-158,500	7.26
Option bonds outstanding on Dec. 31, 2012	**387,750**	**3.92**
Granted option bonds	-	-
Exercised option bonds	-	-
Forfeited option bonds	-3,000	9.79
Expired option bonds	-384,750	3.88
Option bonds outstanding on Dec. 31, 2013	**-**	**-**

Due to legal reasons, the existing option bonds program has been revoked in 2013.

Stock Appreciation Rights (Plan XI)

	Number of stock appreciation rights	Weighted average strike price (in EUR)
Stock appreciation rights outstanding on Jan. 1, 2012	**116,300**	**4.50**
Granted stock appreciation rights	-	-
Exercised stock appreciation rights	-1,333	3.07
Forfeited stock appreciation rights	-8,567	3.05
Expired stock appreciation rights	-9,500	7.01
Stock appreciation rights outstanding on Dec. 31, 2012	**96,900**	**4.40**
Granted stock appreciation rights	-	-
Exercised stock appreciation rights	-1,000	2.55
Forfeited stock appreciation rights	-	-
Expired stock appreciation rights	-8,700	8.74
Stock appreciation rights outstanding on Dec. 31, 2013	**87,200**	**3.99**
Of which exercisable	59,852	3.87

The weighted average remaining contractual life for stock appreciation rights outstanding on December 31, 2013, was 2.86 years. The strike price for those stock appreciation rights is between EUR 1.00 and EUR 11.37.

Stock appreciation rights exercised in 2013 had an average share price of EUR 4.01 on the exercise date.

Stock Appreciation Rights (Plan XIa)

All rights from this plan have been issued in the course of the stock option exchange offer on October 1, 2008.

	Number of stock appreciation rights	Weighted average strike price (in EUR)
Stock appreciation rights outstanding on Jan. 1, 2012	**60,399**	**1.75**
Granted stock appreciation rights	-	-
Exercised stock appreciation rights	-12,270	1.75
Forfeited stock appreciation rights	-2,669	1.75
Expired stock appreciation rights	-	-
Stock appreciation rights outstanding on Dec. 31, 2012	**45,460**	**1.75**
Granted stock appreciation rights	-	-
Exercised stock appreciation rights	-5,315	1.75
Forfeited stock appreciation rights	-	-
Expired stock appreciation rights	-	-
Stock appreciation rights outstanding on Dec. 31, 2013	**40,145**	**1.75**
Of which exercisable	40,145	1.75

The weighted average remaining contractual life for stock appreciation rights outstanding on December 31, 2013, was 1.85 years. The strike price for those stock appreciation rights is EUR 1.75.

Stock appreciation rights exercised in 2013 had an average share price of EUR 3.94 on the exercise date.

Stock Appreciation Rights (Plan XIII)

	Number of stock appreciation rights	Weighted average strike price (in EUR)
Stock appreciation rights outstanding on Jan. 1, 2012	**135,200**	**2.59**
Granted stock appreciation rights	-	-
Exercised stock appreciation rights	-12,600	2.55
Forfeited stock appreciation rights	-300	2.55
Expired stock appreciation rights	-	-
Stock appreciation rights outstanding on Dec. 31, 2012	**122,300**	**2.59**
Granted stock appreciation rights	-	-
Exercised stock appreciation rights	-21,900	2.55
Forfeited stock appreciation rights	-	-
Expired stock appreciation rights	-	-
Stock appreciation rights outstanding on Dec. 31, 2013	**100,400**	**2.60**
Of which exercisable	100,400	2.60

The weighted average remaining contractual life for stock appreciation rights outstanding on December 31, 2013, was 2.08 years. The strike price for those stock appreciation rights is between EUR 2.55 and EUR 3.88.

Stock appreciation rights exercised in 2013 had an average share price of EUR 4.06 on the exercise date.

Stock Option Program 2011 (Plan XIV)

	Number of options	Weighted average strike price (in EUR)
Options outstanding on Jan. 1, 2012	**625,700**	**3.59**
Granted options	443,500	5.04
Exercised options	-	-
Forfeited options	-32,500	3.66
Expired options	-	-
Options outstanding on Dec. 31, 2012	**1,036,700**	**4.21**
Granted options	226,500	3.96
Exercised options	-	-
Forfeited options	-121,000	4.23
Expired options	-	-
Options outstanding on Dec. 31, 2013	**1,142,200**	**4.16**
Of which exercisable	-	-

The average fair value of option rights granted in 2013 is EUR 1.91.

The weighted average remaining contractual life for option rights outstanding on December 31, 2013, was 5.44 years. The strike price for those options is between EUR 3.57 and EUR 5.05.

Stock Option Program 2011 for the Management Board (Plan XIVa)

	Number of options	Weighted average strike price (in EUR)
Options outstanding on Jan. 1, 2012	**-**	**-**
Granted options	200,000	5.05
Exercised options	-	-
Forfeited options	-	-
Expired options	-	-
Options outstanding on Dec. 31, 2012	**200,000**	**5.05**
Granted options	130,000	3.90
Exercised options	-	-
Forfeited options	-50,000	5.05
Expired options	-	-
Options outstanding on Dec. 31, 2013	**280,000**	**3.61**
Of which exercisable	-	-

The average fair value of option rights granted in 2013 is EUR 1.63.

The weighted average remaining contractual life for option rights outstanding on December 31, 2013, was 5.28 years. The strike price for those options is between EUR 3.90 and EUR 5.05.

Stock Appreciation Rights (Plan XV)

	Number of stock appreciation rights	Weighted average strike price (in EUR)
Stock appreciation rights outstanding on Jan. 1, 2012	**153,300**	**3.57**
Granted stock appreciation rights	-	-
Exercised stock appreciation rights	-	-
Forfeited stock appreciation rights	-5,500	3.57
Expired stock appreciation rights	-	-
Stock appreciation rights outstanding on Dec. 31, 2012	**147,800**	**3.57**
Granted stock appreciation rights	-	-
Exercised stock appreciation rights	-	-
Forfeited stock appreciation rights	-3,000	3.57
Expired stock appreciation rights	-	-
Stock appreciation rights outstanding on Dec. 31, 2013	**144,800**	**3.57**
Of which exercisable	-	-

The weighted average remaining contractual life for stock appreciation rights outstanding on December 31, 2013, was 4.73 years. The strike price for those stock appreciation rights is EUR 3.57.

Stock Appreciation Rights (Plan XVI)

All stock appreciation rights in this plan arose from the revocation of option bonds on April 1, 2013.

	Number of stock appreciation rights	Weighted average strike price (in EUR)
Stock appreciation rights outstanding on Dec. 31, 2012	**-**	**-**
Granted stock appreciation rights	103,000	1.53
Exercised stock appreciation rights	-14,000	1.27
Forfeited stock appreciation rights	-	-
Expired stock appreciation rights	-	-
Stock appreciation rights outstanding on Dec. 31, 2013	**89,000**	**1.58**
Of which exercisable	89,000	1.58

The average fair value of stock appreciation rights arisen from the revocation of option bonds (Plan X) valued on December 31, 2013, is EUR 2.21.

The weighted average remaining contractual life for stock appreciation rights outstanding on December 31, 2013, was 1.71 years. The strike price for those stock appreciation rights is between EUR 1.06 and EUR 2.57.

Stock appreciation rights exercised in 2013 had an average share price of EUR 4.22 on the exercise date.

Compensation expenses arising from share-based compensation programs included in operating income were as follows:

(in thousands of EUR)	2013	2012
Plan IX	114	304
Plan IXa	0	242
Plan IXb	47	99
Plan X	-	-
Plan XI	2	5
Plan XIa	6	-9
Plan XIII	6	45
Plan XIV	620	364
Plan XIVa	9	39
Plan XV	63	57
Plan XVI	9	-
Expense from cash settlement of stock appreciation rights and another share-based compensation programs	37	198
	913	**1.344**

The liability arising from stock appreciation rights is included in non-current provisions and amounts to EUR 660 thousand and EUR 446 thousand on December 31, 2013 and 2012, respectively. The intrinsic value of those liabilities amounts to EUR 426 thousand on December 31, 2013 (prior year: EUR 178 thousand).

(32) Employees

In 2013 and 2012, respectively, the ADVA Optical Networking Group had an average of 1,413 and 1,322 permanent employees and an average of 14 and 15 apprentices on its payroll. The employee breakdown by department is listed below:

	2013	2012
Research and development	646	581
Purchasing and production	203	206
Quality management	21	21
Sales, marketing and service	394	372
Management and administration	149	142
Apprentices	14	15
	1,427	**1,337**

A further 12 and 13 people were employed on a temporary basis effective December 31, 2013 and 2012, respectively.

Personnel expenses for 2013 and 2012 totaled EUR 112,766 thousand and EUR 105,499 thousand, respectively:

(in thousands of EUR)	2013	2012
Wages and salaries	95,450	89,448
Social security costs	15,443	13,817
Expenses for defined contribution plans	960	890
Share-based compensation expenses	913	1,344
	112,766	**105,499**

Retirement Benefit Schemes
The Group operates various defined contribution retirement benefit schemes in several Group companies. The assets of the schemes are held separately from those of the Group in funds under the control of trustees. The only obligation of ADVA Optical Networking with respect to the retirement benefit scheme is to make the specified contributions. Payments to defined contribution retirement benefit schemes are charged as an expense as they fall due. Payments made to state-managed retirement benefit schemes are dealt with as payments to defined contribution schemes where the Group's obligations under the schemes are equivalent to those arising in a defined contribution retirement benefit scheme.

(33) Related Party Transactions

EGORA Holding GmbH, Martinsried/Munich, and its subsidiaries (the EGORA Group), OptXCon Inc., Saguna Networks Ltd. and all members of the Company's governing bodies and their relatives qualify as related parties to ADVA Optical Networking on December 31, 2013, in the sense of IAS 24.

On December 31, 2013, the EGORA Group held an 18.0% equity stake in ADVA Optical Networking.

On November 1, 2012, ADVA Optical Networking SE acquired 10% of the shares of Saguna Networks Ltd., Nesher, Israel. Christoph Glingener is a board member of the company. A service agreement with Saguna Networks Ltd. exists regarding the provision of development services for the companies of ADVA Optical Networking Group. In 2013 and 2012, no repective sevices were provided by Saguna Networks Ltd.

In 2013 and 2012, ADVA Optical Networking did not sell any products to the EGORA Group. During the same period, ADVA Optical Networking acquired components from the EGORA Group.

ADVA Optical Networking has entered into several agreements with the EGORA Group under which ADVA Optical Networking is entitled to make use of certain facilities and services of the EGORA Group.

All transactions with the related parties listed above are conducted on an arm's-length basis.

A summary of transactions with related parties is provided in the table below:

(in thousands of EUR)	2013	2012
Purchases from related parties		
EGORA Group	39	9
	39	**9**
Services provided by related parties		
EGORA Group	-	2
	-	**2**

On December 31, 2013 and 2012, respectively, no trade receivables, provisions and trade payables in respect to related parties existed.

In 2013, ADVA Optical Networking SE granted a loan of USD 310 thousand (EUR 229 thousand) to Saguna Networks Ltd.

See note (34) for detailed information about compensation of the Management Board and the Supervisory Board.

(34) Governing Boards and Compensation

Management Board

	Resident in	External mandates
Brian Protiva *Chief Executive Officer*	Berg, Germany	-
Christoph Glingener *Chief Technology Officer*	Jade, Germany	Member of the Board of Saguna Networks Ltd., Nesher, Israel
Jaswir Singh *Chief Financial Officer & Chief Operating Officer*	Alpharetta (Georgia), USA	-

Supervisory Board

	Resident in	Occupation	External mandates
Anthony Maher *Chairman*	Munich, Germany	Managing Director, Belmondo Capital, Inc., Munich, Germany	-
Johanna Hey *Vice Chairwoman*	Cologne, Germany	Professor for Tax Law, University of Cologne, Cologne, Germany	Member of the Central Advisory Board of Commerzbank AG, Frankfurt am Main, Germany
Eric Protiva	Atherton (California), USA	Managing Director, EGORA Holding GmbH, Martinsried/Munich, Germany	Member of the Supervisory Board of AMS Technologies AG, Martinsried/Munich, Germany Member of the Board of Directors of Elforlight Ltd., Daventry, United Kingdom

Compensation of the Management Board

The total Management Board compensation was EUR 1,527 thousand in 2013 and EUR 1,850 thousand in 2012. This amount is analyzed across the individual Board members as follows:

(in thousands of EUR)	Fixed	Variable	Total 2013	Total 2012
Brian Protiva *Chief Executive Officer*	273	178	451	516
Christoph Glingener *Chief Technology Officer*	271	122	393	432
Jaswir Singh *Chief Financial Officer &* *Chief Operating Officer*	339	86	425	469
Christian Unterberger *Chief Sales & Marketing Officer* *(until March 31, 2013)*	68	190	258	433

At the end of Q1 2013, Christian Unterberger left the Company by mutual agreement. Brian Protiva has assumed his areas of responsibility. A compensation of EUR 160 thousand has been agreed in a non-competition clause for the twelve months after his departure. The amount is included in variable compensation in the table above. Payment is due in four equal instalments at the end of each quarter following his departure. The final payment of EUR 40 thousand due in March 2014 is included in other current liabilities.

The fixed compensation includes contributions to unemployment insurance, statutory pension insurance and company car allowances.

The estimated variable compensation relates to the performance-based bonus for 2013, which is included in other current liabilities on December 31, 2013.

The Group paid pecuniary damage liability insurance premiums on behalf of members of the Management Board totaling EUR 12 thousand both in 2013 and 2012 (in equal amounts for each Management Board member), respectively.

In 2013 and 2012, no loans or prepayments were granted to the members of the Management Board.

On December 31, the members of the Management Board held the following shares and had been granted the following stock options:

	Shares		**Stock options**	
	2013	**2012**	**2013**	**2012**
Brian Protiva *Chief Executive Officer*	294,030	294,030	275,000	275,000
Christoph Glingener *Chief Technology Officer*	-	-	325,000	325,000
Jaswir Singh *Chief Financial Officer &* *Chief Operating Officer*	-	-	300,000	300,000

The options to members of the Management Board were granted out of Plan IX, Plan IXb and Plan XIVa. These option rights authorize the Management Board to purchase the said number of common shares in the Company once the qualifying period has elapsed. Plan IXb and Plan XIVa include a profit limit of EUR 20.00 per option, whereas Plan IX has no profit limitations.

The strike price for these option rights is
- EUR 2.57 for 270,000 options granted on July 1, 2008,
- EUR 2.26 for 130,000 options granted on October 1, 2009,
- EUR 2.55 for 145,000 options granted on January 1, 2010,
- EUR 5.04 for 75,000 options granted on October 1, 2010,
- EUR 5.05 for 150,000 options granted on August 15, 2012,
- EUR 3.90 for 130,000 options granted on November 15, 2013, respectively.

Compensation of the Supervisory Board

The fixed compensation to be paid to the Supervisory Board for 2013 and 2012 totaled EUR 235 thousand and EUR 270 thousand, respectively. This amount can be analyzed across the individual Board members as follows:

(in thousands of EUR)	Fixed 2013	Fixed 2012	Variable 2012	Total 2012
Anthony Maher *Chairman*	100	89	7	96
Johanna Hey *Vice Chairwoman (since July 23, 2012)*	90	62	6	68
Eric Protiva	45	42	3	45
Thomas Smach *(until July 23, 2012)*	-	45	6	51
Albert Rädler ✝ *(until February 25, 2012)*	-	6	1	7
Nikolaus Zwick *(March 30 until July 23, 2012)*	-	13	1	14
Frank Fischer *(March 30 until July 23, 2012)*	-	13	1	14

The fixed compensation for the Supervisory Board of ADVA Optical Networking SE for 2013 amounting to EUR 235 thousand is paid out in quarterly installments. The fixed compensation for Q4 2013 amounting to EUR 58 thousand was paid out in January 2014. In the consolidated financial statements, this amount is recognized in liabilities. As a result of the change of the remuneration system concluded in the Annual Shareholders' Meeting on June 4, 2013, the members of the Supervisory Board do not receive any variable compensation after July 23, 2012 (date of the conversion of ADVA AG Optical Networking into an SE legal entity).

The fixed compensation for the Supervisory Board of ADVA AG Optical Networking for the period ending July 23, 2012, of EUR 166 thousand and for the Supervisory Board of ADVA Optical Networking SE for the period starting July 23, 2012, of EUR 104 thousand has been paid out in 2012 and 2013. Furthermore, the Annual Shareholders' meeting approved variable compensation of EUR 25 thousand for the Supervisory Board of ADVA AG Optical Networking for 2012. This variable compensation was paid out in 2013. At December 31, 2012, the compensation for 2012 that was only paid out in the following year has been recognized in provisions.

The Group paid pecuniary damage liability insurance premiums on behalf of members of the Supervisory Board totaling EUR 12 thousand and EUR 19 thousand in 2013 and 2012, respectively.

On December 31, members of the Supervisory Board held the following shares:

	Shares	
	2013	2012
Anthony Maher *Chairman*	8,000	8,000
Johanna Hey *Vice Chairwoman*	-	-
Eric Protiva	320,000	320,000

(35) Events After the Balance Sheet Date

There were no events after the balance sheet date that affected the financial position of the Group on December 31, 2013 or its financial performance for the year then ended, nor were there any events considered material for disclosure.

Declaration of compliance with the German Corporate Governance Code

Pursuant to Section 161 of the German Stock Corporation Law (AktG), the Management Board and the Supervisory Board have issued a declaration of compliance with the German Corporate Governance Code. This declaration is published on the Group's website (www.advaoptical.com).

Meiningen, February 17, 2014

Brian Protiva

Christoph Glingener

Jaswir Singh

Affirmative Declaration of the Legal Representatives

We, the members of the Management Board of ADVA Optical Networking SE, to the best of our knowledge affirm that, in accordance with the applicable reporting principles, the management report and the consolidated financial statements of the ADVA Optical Networking Group represent a true and fair view of the net assets, financial position and performance of the Group, together with a description of the principal opportunities and risks associated with the expected development of the Group.

Meiningen, February 17, 2014

Brian Protiva

Christoph Glingener

Jaswir Singh

Independent Auditor's Opinion

The following independent auditor's opinion is a mere convenience translation from the German language and hence does not bear the auditor's seal and signatures. The German language version of the independent auditor's opinion only refers to the German language version of the consolidated 2013 IFRS financial statements and Group management report of ADVA Optical Networking SE.

Auditor's Report

We have audited the consolidated financial statements prepared by the ADVA Optical Networking SE, Meiningen, comprising the statement of financial position, the income statement, the statement of comprehensive income, statement of changes in equity, cash flow statement and the notes to the consolidated financial statements, together with the group management report for the business year from January 1 to December 31, 2013. The preparation of the consolidated financial statements and the group management report in accordance with the IFRSs, as adopted by the EU, and the additional requirements of German commercial law pursuant to § (Article) 315a Abs. (paragraph) 1 HGB ("Handelsgesetzbuch": German Commercial Code) is the responsibility of the parent Company's Board of Managing Directors. Our responsibility is to express an opinion on the consolidated financial statements and on the group management report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with § 317 HGB and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (Institute of Public Auditors in Germany) (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with the applicable financial reporting framework and in the group management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the group management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of those entities included in consolidation, the determination of the entities to be included in consolidation, the accounting and consolidation principles used and significant estimates made by the Company's Board of Managing Directors, as well as evaluating the overall presentation of the consolidated financial statements and the group management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion based on the findings of our audit the consolidated financial statements comply with the IFRSs as adopted by the EU, and the additional requirements of German commercial law pursuant to § 315a Abs. 1 and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with these requirements. The group management report is consistent with the consolidated financial statements and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Munich, February 18, 2014

PricewaterhouseCoopers
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

sgd. Alexander Winter
Wirtschaftsprüfer
(German Public Auditor)

sgd. ppa. Sven Jacob
Wirtschaftsprüfer
(German Public Auditor)

Additional Information

Can Operational Excellence be Measured?

Our customers compete in some of the most fiercely competitive markets in the world and must be confident that we can deliver what they need, when they need it. For us, operational excellence is not just an empty promise. It is something we can quantify. In 2013, we won a prestigious Supply Chain Management Award. This annual award is presented to the company with the most effective value chain in the manufacturing industry. The awarding bodies believed that our global end-to-end and cross-enterprise segmentation is unique and provides us with a clear competitive edge. An edge that we leverage for our customers.

Quarterly Overview 2011–2013

(IFRS, in thousands of EUR, except stated otherwise)	2011				2012				2013			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
INCOME STATEMENT												
Revenues	**70,351**	**77,837**	**79,325**	**83,432**	**81,655**	**85,879**	**82,267**	**80,268**	**77,034**	**78,367**	**79,064**	**76,237**
Pro forma cost of goods sold pre amortization for capitalized development expenses	-41,368	-44,399	-44,830	-46,832	-46,068	-46,877	-45,687	-42,794	-43,586	-42,665	-43,319	-41,232
Amortization for capitalized development expenses	-3,523	-3,747	-3,594	-3,267	-3,320	-3,902	-4,255	-3,917	-3,679	-4,407	-4,666	-5,007
Pro forma gross profit*	**25,460**	**29,691**	**30,901**	**33,333**	**32,267**	**35,100**	**32,325**	**33,557**	**29,769**	**31,295**	**31,079**	**29,998**
Pro forma selling and marketing expenses	-10,033	-11,099	-10,983	-11,296	-10,791	-11,761	-10,712	-12,995	-11,685	-12,607	-11,531	-10,894
Pro forma general and administrative expenses	-6,086	-6,183	-6,273	-5,465	-6,781	-6,707	-6,123	-6,114	-6,673	-6,874	-5,958	-6,720
Pro forma research and development expenses	-14,359	-14,094	-14,782	-16,848	-16,776	-16,613	-16,151	-15,515	-16,842	-16,762	-15,868	-16,177
Income from capitalization of development expenses	5,211	4,907	6,133	7,397	6,053	6,446	5,966	5,064	5,580	6,001	5,959	4,950
Other operating income and expenses, net	714	277	469	291	513	382	324	840	656	483	294	1,098
Pro forma operating income	**907**	**3,499**	**5,465**	**7,412**	**4,485**	**6,847**	**5,629**	**4,837**	**805**	**1,536**	**3,975**	**2,255**
Amortization of intangible assets from acquisitions	-632	-607	-614	-640	-653	-662	-160	-145	-171	-170	-171	-171
Stock compensation expenses	-582	-479	-424	-98	-318	-287	-335	-404	-252	-213	-275	-173
Operating income (loss)	**-307**	**2,413**	**4,427**	**6,674**	**3,514**	**5,898**	**5,134**	**4,288**	**382**	**1,153**	**3,529**	**1,911**
Interest income and expenses, net	-342	-409	-402	-378	-418	-213	-234	-298	-152	-262	-427	-303
Other financial gains and losses, net	-1,609	-988	2,988	1,937	-842	1,850	-36	-138	-756	-179	-75	-465
Income (loss) before tax	**-2,258**	**1,016**	**7,013**	**8,233**	**2,254**	**7,535**	**4,864**	**3,852**	**-526**	**712**	**3,027**	**1,143**
Income tax benefit (expense), net	-56	-179	2,719	451	1,790	-2,436	-1,386	249	1,286	-588	-771	1,224
Net income (loss)	**-2,314**	**837**	**9,732**	**8,684**	**4,044**	**5,099**	**3,478**	**4,101**	**760**	**124**	**2,256**	**2,367**
Earnings per share in EUR												
basic	-0.05	0.02	0.21	0.18	0.09	0.11	0.07	0.09	0.02	0.00	0.05	0.05
diluted	-0.05	0.02	0.20	0.18	0.08	0.10	0.07	0.08	0.02	0.00	0.05	0.05
BALANCE SHEET (as of period end)												
Cash and cash equivalents	44,712	55,375	55,991	59,110	63,999	69,869	70,329	70,625	65,310	80,332	80,637	80,934
Inventories	36,085	32,135	34,900	36,536	36,030	37,529	40,013	41,339	39,267	40,669	44,356	40,074
Goodwill	19,273	19,097	19,458	19,842	19,742	20,167	20,132	19,876	19,898	20,011	19,925	19,875
Capitalized R&D expenses	31,182	32,261	34,911	39,231	41,988	44,748	46,511	47,497	49,238	50,778	52,126	52,080
Other intangible assets	7,644	6,718	6,216	5,541	4,638	4,153	3,930	3,586	3,985	3,612	3,098	2,699
Total intangible assets	58,099	58,076	60,585	64,614	66,368	69,068	70,573	70,959	73,121	74,401	75,149	74,654
Other assets	73,949	81,099	99,276	99,636	89,912	96,503	94,005	101,172	109,112	99,879	96,031	97,416
Total assets	212,845	226,685	250,752	259,896	256,309	272,969	274,920	284,095	286,810	295,281	296,173	293,078
Total stockholders' equity	111,809	112,125	124,424	135,986	139,336	147,733	151,484	153,909	156,118	154,822	155,987	157,820
CASH FLOW STATEMENT												
Cash flow from operating activities	-1,078	18,144	9,718	12,952	13,535	12,729	9,205	9,687	1,697	12,838	9,860	7,018
Gross capital expenditures for property, plant and equipment	-928	-1,897	-1,543	-2,892	-2,067	-1,550	-2,573	-2,977	-1,512	-1,831	-1,717	-1,929
EMPLOYEES (as of period end)	1,224	1,257	1,275	1,304	1,317	1,323	1,354	1,378	1,427	1,430	1,427	1,425

Pro forma financial numbers exclude non-cash charges related to the stock compensation programs and amortization and impairment of goodwill and acquisition-related intangible assets.

*From 2012, amortization for capitalized development projects is presented as cost of goods sold; prior period information has been adjusted accordingly.

Multi-Year Overview 2003–2013

(in thousands of EUR, except stated otherwise)	2003 U.S. GAAP	2004 U.S. GAAP	2005 IFRS	2006 IFRS	2007 IFRS	2008 IFRS	2009 IFRS	2010 IFRS	2011 IFRS	2012 IFRS	2013 IFRS	Change 2013 vs. 2012
INCOME STATEMENT												
Revenues	**90,440**	**102,136**	**131,292**	**192,709**	**251,486**	**217,672**	**232,808**	**291,725**	**310,945**	**330,069**	**310,702**	**-6%**
Pro forma cost of goods sold pre amortization for capitalized development expenses	-45,517	-51,387	-67,555	-109,630	-151,050	-125,802	-132,851	-170,501	-177,429	-181,426	-170,802	-6%
Amortization for capitalized development projects	0	0	-974	-1,219	-7,724	-3,052	-7,190	-11,373	-14,131	-15,394	-17,759	+15%
Pro forma gross profit*	**44,923**	**50,749**	**62,763**	**81,860**	**92,712**	**88,818**	**92,767**	**109,851**	**119,385**	**133,249**	**122,141**	**-8%**
Pro forma general, administrative, selling and marketing expenses	-23,460	-26,542	-34,325	-46,721	-59,685	-60,385	-60,005	-66,224	-67,418	-71,984	-72,942	+1%
Pro forma research and development expenses	-12,026	-12,088	-15,238	-28,054	-41,372	-40,682	-40,714	-49,391	-60,083	-65,055	-65,649	+1%
Income from capitalization of development expenses	0	736	5,805	5,852	10,039	12,056	12,404	15,291	23,648	23,529	22,490	-4%
Restructuring expenses	0	0	0	0	0	-2,251	0	0	0	0	0	-
Other operating income and expenses, net	0	0	89	185	86	1,736	1,650	3,761	1,751	2,059	2,531	+23%
Pro forma operating income (loss)	**9,437**	**12,855**	**19,094**	**13,122**	**1,780**	**-708**	**6,102**	**13,288**	**17,283**	**21,798**	**8,571**	**-61%**
Amortization of intangible assets from acquisitions excluding goodwill	-4,636	-3,084	-714	-6,681	-10,727	-4,574	-2,443	-2,141	-2,493	-1,620	-683	-58%
Impairment of goodwill	0	0	0	0	-6,581	0	0	0	0	0	0	-
Stock compensation expenses	-1,071	-1,284	-1,198	-5,526	-3,186	-1,761	-1,378	-1,848	-1,583	-1,344	-913	-32%
Operating income (loss)	**3,730**	**8,487**	**17,182**	**915**	**-18,714**	**-7,043**	**2,281**	**9,299**	**13,207**	**18,834**	**6,975**	**-63%**
Interest income and expenses, net	-769	-192	-26	-490	-853	-1,005	-1,215	-1,439	-1,531	-1,163	-1,144	-2%
Other financial gains and losses, net	-484	-531	248	-1,443	-1,734	-1,103	543	3,130	2,328	834	-1,475	-
Income (loss) before tax	**2,477**	**7,764**	**17,404**	**-1,018**	**-21,301**	**-9,151**	**1,609**	**10,990**	**14,004**	**18,505**	**4,356**	**-76%**
Income tax benefit (expense), net	2,354	-537	-5,530	-9,325	-8,154	275	-289	-3,983	2,935	-1,783	1,151	-
Loss from discontinued operations, after tax	46	0	0	0	0	0	0	0	0	0	0	-
Net income (loss)	**4,877**	**7,227**	**11,874**	**-10,343**	**-29,455**	**-8,876**	**1,320**	**7,007**	**16,939**	**16,722**	**5,507**	**-67%**
Earnings per share in EUR												
basic	0.15	0.22	0.35	-0.26	-0.64	-0.19	0.03	0.15	0.36	0.35	0.11	-69%
diluted	0.15	0.21	0.34	-0.26	-0.64	-0.19	0.03	0.15	0.35	0.34	0.11	-68%
BALANCE SHEET (as of December 31)												
Cash and cash equivalents	18,819	24,054	27,657	32,181	41,576	46,560	50,882	54,085	59,110	70,625	80,934	+15%
Inventories	8,561	12,964	14,373	42,034	31,029	26,961	25,400	39,588	36,536	41,339	40,074	-3%
Goodwill	8,955	11,046	11,704	24,247	20,006	18,854	19,103	19,653	19,842	19,876	19,875	0%
Capitalized R&D expenses	0	736	5,567	10,198	12,238	19,829	25,449	29,571	39,231	47,497	52,080	+10%
Other intangible assets	2,434	2,930	3,132	28,107	18,178	12,926	9,991	7,467	5,541	3,586	2,699	-25%
Total intangible assets	11,389	14,712	20,403	62,552	50,422	51,609	54,543	56,691	64,614	70,959	74,654	+5%
Other assets	38,646	47,474	62,634	95,918	80,769	70,670	66,172	83,758	99,636	101,172	97,416	-4%
Total assets	77,415	99,204	125,067	232,685	203,796	195,800	196,997	234,122	259,896	284,095	293,078	+3%
Total stockholders' equity	49,920	63,543	79,681	138,322	109,026	97,998	101,270	115,414	135,986	153,909	157,820	+3%
CASH FLOW STATEMENT												
Cash flow from operating activities	14,523	6,590	13,526	-7,899	25,150	23,343	29,105	21,100	39,736	45,156	31,413	-30%
Gross capital expenditures for property, plant and equipment	-2,528	-3,007	-5,008	-10,245	-8,378	-4,464	-5,807	-8,808	-7,260	-9,167	-6,989	-24%
EMPLOYEES (as of December 31)	428	496	561	853	1,040	1,042	1,100	1,203	1,304	1,378	1,425	+3%

Pro forma financial numbers exclude non-cash charges related to the stock compensation programs and amortization and impairment of goodwill and acquisition-related intangible assets.

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Glossary

Agile Core
Agile core is a marketing term used by ADVA Optical Networking to promote the enhanced level of flexibility and automation in the FSP 3000 platform for applications in the network core. The Company's agile core express solution is optimized for 100G coherent transmission technology, providing unprecedented capacity, flexibility, and reach.

ATM (Asynchronous Transfer Mode)
ATM is a network protocol that encodes data traffic into small fixed-sized cells instead of variable-sized packets, as in packet-switched networks like Ethernet.

Broadband Remote Access Server
A broadband remote access server is a network element routing traffic to and from broadband remote access devices such as DSL access multiplexers on an Internet service provider's network. See also DSL (Digital Subscriber Line).

Cachejack™
This innovative concept loads popular content on integrated cache servers near the mobile base station. That content is then delivered from a cache server, which is in closer proximity to the requesting user than the mobile core network. The effect is reduced time to first byte, translating into an enhanced user experience as subscribers receive content more quickly. In addition, Cachejack™ enables monetized location-based service offerings; for example, advertisements tailored to a user's precise location can be delivered along with requested content. And Cachejack™ helps operators save bandwidth and money by optimizing mobile backhaul.

Carriers
Carriers, in general, are companies that build and maintain communications networks for commercial use. Beyond incumbent telephony companies, these also include new alternative carriers, which were established during the deregulation of the telecommunications market, and special service providers, which offer outsourced services (e.g., software applications or data storage) for enterprise customers.

Cloud
Cloud in the context of IT describes a concept where applications no longer run on the user's in-house IT infrastructure (for example, a server) but are outsourced to a service provider whose IT infrastructure is not visible or known in detail – as if it was hidden in a cloud. A typical example is the use of software as a service, where the software is not stored on the user's machine, but on servers of the software service provider.

Control Plane
Within a network, the control plane is software that manages the establishment, maintenance and termination of connections and services.

CWDM (Coarse Wavelength Division Multiplexing)
CWDM is a standardized WDM technology that uses up to 20 different wavelengths for data transmission over a single fiber. In contrast to DWDM, CWDM uses only a 'coarse' wavelength grid, so the underlying optical component technology is simpler. This makes CWDM systems very cost-effective, but also limits them in terms of total capacity. See also DWDM (Dense Wavelength Division Multiplexing) and WDM (Wavelength Division Multiplexing).

DSL (Digital Subscriber Line)
DSL is a technology that provides fast digital data transmission over the copper wires of a local telephone network. The advantage of DSL is that broadband services like fast Internet access and Internet television signals can be delivered over the same twisted pair of copper wires that was originally deployed for phone service only.

DWDM (Dense Wavelength Division Multiplexing)
DWDM is a standardized WDM technology that uses up to 192 different wavelengths for data transmission over a single fiber. DWDM uses a 'dense' wavelength grid that requires high-precision optical components, maximizing the bandwidth per fiber. See also CWDM (Coarse Wavelength Division Multiplexing) and WDM (Wavelength Division Multiplexing).

Etherjack™
This innovative ADVA Optical Networking technology allows carriers to deploy differentiated Ethernet services by providing the industry's first intelligent Ethernet demarcation point, which includes service definition toward the end-user and end-to-end quality-of-service assurance across any network.

Ethernet
Ethernet is a packet-based data transmission protocol with a data rate of 10Mbit/s. Fast Ethernet provides a data rate of 100Mbit/s, Gigabit Ethernet 1Gbit/s and 10 Gigabit Ethernet 10Gbit/s. Today also 40 and 100 Gigabit Ethernet solutions are commercially available with data rates of 40Gbit/s and 100Gbit/s, respectively.

FC (Fibre Channel)
Fibre Channel, or FC, has been designed for the continuous, serial high-speed transmission of big data volumes. It is primarily used for SANs in enterprise storage. Today's transmission speeds include 1, 2, 4, 8, 10 and 16Gbit/s. See also SAN (Storage Area Network).

Frame Relay
Frame Relay is an efficient data transmission technique. Network providers commonly sell Frame Relay services as a lower-cost alternative to leased lines. With Frame Relay, service providers can sell more total bandwidth than they have available in their networks because not all users use 100% of their bandwidth all the time.

FSP (Fiber Service Platform)
The Fiber Service Platform is ADVA Optical Networking's comprehensive product portfolio that provides carriers and enterprises with Optical+Ethernet solutions for access, metro and long-haul networks.

FTTx (Fiber-To-The-x)
FTTx is an umbrella term for fiber-based access networks, where x defines the end point of the fiber network. One example is FTTC (Fiber-To-The-Curb) where the fiber network is terminated in a street cabinet (at the curb) and the remaining distance to the end user is bridged by some other – in most cases existing – media, such as copper. Many network operators see FTTH (Fiber-To-The-Home) as the ultimate solution. In a FTTH scenario the fiber is deployed all the way to individual homes.

Gbit/s or G (Gigabit per second)
Bits are binary symbols of zero or one and are the standard unit by which data is stored and processed by computers. “Giga” stands for one billion (1,000,000,000). Bit/s is the basic unit of a data rate, which describes how many bits per second are being transmitted. One Gbit/s or G is therefore a data rate that transmits one billion bits of data per second.

GMPLS (Generalized Multiprotocol Label Switching)
GMPLS extends MPLS to provide the control plane (signaling and routing) for devices that switch data. This common control plane simplifies network operation and management by automating end-to-end provisioning of connections, managing network resources and providing the quality of service level that is expected in advanced applications. See also MPLS (Multiprotocol Label Switching).

IEEE 1588v2 Mini-Grandmaster Clock
The Precision Time Protocol (PTP) is used to synchronize clocks throughout a computer network. PTP was originally defined in the Institute of Electrical and Electronic Engineers’ IEEE 1588-2002 standard and revised in 2008 as PTP version 2 (1588v2) for improved accuracy, precision and robustness. The 1588v2 is used in carrier networks to synchronize clocks over a data transport infrastructure. A grandmaster clock is the root timing reference in a hierarchical architecture, typically located centrally in a network. A mini-grandmaster clock is a smaller version of a root timing reference, typically located further out in the network.

IP (Internet Protocol)
IP is a packet-based method by which data is sent from one computer to another on the Internet.

ISO 14001
ISO 14001 is a standard developed and published by the International Organization for Standardization. This standard defines, establishes and maintains an environmental management system for the manufacturing and service industries.

LAN (Local Area Network)
A LAN is a computer network covering a small physical area, like an office or small group of buildings. There are several technologies available for setting up a LAN. Today, Ethernet is the most commonly used technology in LAN environments. See also Ethernet.

LTE (Long Term Evolution) / LTE-Advanced
LTE is the project name of a high-performance air interface for cellular mobile communication systems. It is often used as the synonym for the 4th generation (4G) of radio technologies designed to increase the capacity and speed of mobile networks. LTE-Advanced provides further enhancements to the LTE technology, enabling operators to deliver even more bandwidth to more mobile users.

MPLS (Multiprotocol Label Switching)
MPLS enables packet-switched transmission of data packets in a connection-less network along a pre-configured path. This data-carrying mechanism is mostly used by carriers with large transport networks and Internet Protocol-based voice and data services.

MSO (Multiple Service Operator)
The term MSO emerged in the 1990s when cable television companies, mainly in the U.S., started to offer telecom services in addition to their traditional television and video offerings. Technically, most telecom service providers today could be called multiservice operators, but the term MSO still implies the historical roots in the cable television space.

NFV (Network Functions Virtualization)
NFV is an alternative design approach for building complex IT applications, particularly in the telecommunications and service provider industries. NFV virtualizes entire classes of functions into building blocks that may be connected, or chained, together to create services. With the introduction of NFV the architecture of service provider networks will change. Functions that were previously tied to a particular network element can now hosted centrally leading to a new distribution of hardware and software functionality across networks.

OAM & P (Operations, Administration, Maintenance & Provisioning) Capabilities
Capabilities that control and manage data transport in carrier networks. Enhanced OAM & P capabilities facilitate specific service level agreements between carriers and their customers detailing data signal quality and speed.

OEM (Original Equipment Manufacturer)
OEM partners purchase products from other companies to fill gaps in their portfolio and offer an end-to-end solution. They typically re-label and market the products under their own brand name.

OpenFlow
OpenFlow is an open standard protocol that gives access to the forwarding plane of a network switch or router. Separating the control plane from the data forwarding plane is a fundamental principle of SDN. Hence OpenFlow is often seen as an SDN enabler. See also Control Plane and SDN (Software-Defined Networking).

OTN (Optical Transport Network)
The ITU-T (Telecommunication Standard Sector of the International Telecommunication Union) recommendation G.709 is commonly called OTN. It was created with the intention of combining the benefits of SONET/SDH technology with the bandwidth expansion capabilities offered by DWDM technology. OTN functionality is often embraced by carriers operating a large wide area network. See also SONET (Synchronous Optical Network) / SDH (Synchronous Digital Hierarchy) and DWDM (Dense Wavelength Division Multiplexing).

PON (Passive Optical Network)
PON is a concept for fiber-based access networks. Using unpowered optical splitters, a point-to-multipoint topology is set up, enabling the efficient connection of multiple customer end points to one network node.

Protocol
A protocol defines the "language" elements that networks use to communicate with each other.

RAN (Radio Access Network)
The RAN is part of a mobile telecommunication system connecting a mobile communication device such as a mobile phone or smart phone via an air interface to the network of the communication service provider. The most current RAN technology is LTE, a high-speed and low-latency RAN for mobile broadband services. See also LTE (Long Term Evolution) / LTE-Advanced.

RAYcontrol™
This innovative ADVA Optical Networking GMPLS-based control plane technology greatly simplifies the management of optically switched networks and offers unparalleled flexibility in service delivery, protection and restoration capabilities. See also Control Plane and GMPLS (Generalized Multiprotocol Label Switching).

REACH (Registration, Evaluation, Authorization and Restriction of Chemicals)
A regulation issued by the European Union addressing the production and use of chemical substances and the potential impact of these substances on human health and the environment.

ROADM (Reconfigurable Optical Add / Drop Multiplexing)
ROADM is an innovative functionality in optical networks that enables cost-effective switching of wavelengths.

RoHS (Restriction of Hazardous Substances)
A directive issued by the European Union regarding the restriction of specific hazardous substances used for production and processing of electronic devices and components.

SAN (Storage Area Network)
A SAN establishes direct connections between storage devices and network servers, enabling such devices to be shared as peer resources and increasing the capacity and performance of storage hardware.

SDN (Software-Defined Networking)
SDN is an approach to building networks where the control function is separated from the forwarding engine. I.e., SDN decouples the system that makes decisions about where traffic is sent from the underlying hardware that forwards traffic to the selected destination. SDN has the potential to be disruptive to the networking industry and is seen as a key enabler on the road to network virtualization. See also Control Plane and OpenFlow.

Server Virtualization
Server virtualization is the masking of server resources, including the number and identity of individual physical servers, processors and operating systems, from server users. The server administrator uses a software application to divide one physical server into multiple isolated virtual environments, which are made accessible to individual users. These virtual environments function equivalently to a separate physical computer and are sometimes called virtual private servers, but they are also known as guests or instances.

SONET (Synchronous Optical Network) /
SDH (Synchronous Digital Hierarchy)
SONET and SDH are methods for communicating digital information. These methods were developed in the mid-1980s to replace the Plesiochronous Digital Hierarchy system for transporting large amounts of telephone and data traffic and to allow for interoperability between equipment from different vendors. While SONET is a U.S. standard, SDH is dominant in Europe and also widely used in the rest of the world.

Syncjack™
This innovative ADVA Optical Networking technology allows carriers to deliver, monitor and assure accurate timing and synchronization information required for applications such as mobile backhaul.

Sync Probe
Advanced mobile networks rely on precise synchronization of the radio access network. In many cases, it is desirable to deliver timing information via the backhaul network to the base station. A sync probe device enhances the capability of backhaul networks to deliver such information reliably by monitoring and assuring that the timing information is accurate.

TL 9000
TL 9000 is a quality management system standard defined specifically for the telecommunications industry. It standardizes the quality system requirements for the design, development, delivery, installation and maintenance of telecommunication products and services, and it also defines the performance metrics required to measure the situation at the time of the implementation of the standard as well as progress made.

Triple Play Services
Triple play services refer to bundled offerings of data, voice and video services to end customers. These services are offered in a bundle of three, and may include Internet and e-mail access, Internet telephony, Internet television and video-on-demand.

UMTS (Universal Mobile Telecommunications System)
UMTS is one of the third-generation cell phone technologies that support high-bandwidth applications on mobile devices.

Utility Computing
Utility computing describes a concept where an IT service provider offers his customers services such as computing power or storage capacity that are metered and charged based on actual usage. In this concept, computing power and storage capacity are organized and billed like a utility, similar to other utilities such as water, gas or electricity.

VAR (Value Added Reseller)
VAR partners combine products from a number of different vendors together with their own services to offer customers a complete and comprehensive solution.

WDM (Wavelength Division Multiplexing)
WDM expands the capacity of networks by allowing a greater number of signals to be transmitted over a single fiber. WDM enables numerous channels of data to be multiplexed into unique color bands, and then to be combined and transmitted over a single fiber and de-multiplexed at the other end.

WDM-PON (Wavelength Division Multiplexing-Passive Optical Network)
WDM-PON is an innovative concept for access and backhaul networks. It uses multiple wavelengths (WDM) over a physical point-to-multipoint fiber infrastructure that contains no active components (PON). The use of different wavelengths allows for traffic separation within the same physical fiber. The result is a network that provides logical point-to-point connections over a physical point-to-multipoint network topology. A WDM-PON allows operators to deliver high bandwidth to multiple endpoints over long distances. See also PON (Passive Optical Network) and WDM (Wavelength Division Multiplexing).

WEEE (Waste Electrical and Electronic Equipment)
A directive issued by the European Union regarding the return and recycling of waste electrical and electronic equipment waste.

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PDF files of this annual report, as well as quarterly reports, presentations and general investor information, are also located on the Company's website and can be downloaded in both English and German. Quarterly conference calls are conducted on the day of earnings announcements. Related PDF, audio and transcript files are available for download in the investor relations section of the Company's website, www.advaoptical.com.

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