



Mercator



**Summary of the
Annual report for the year
2009**

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MERCATOR GROUP PROFILE

Mercator Group is one of the largest retail chains in the region of Southeastern Europe, the leading retail chain in Slovenia, and increasingly important player in the markets of Serbia, Croatia, Bosnia and Herzegovina, and Montenegro. In 2009, we entered two new markets: Bulgaria and Albania. Our vision remains unchanged – we wish to be the leading retail chain with FMCG program (market program) in Southeastern Europe.



Current markets of our operations: Slovenia, Serbia, Croatia, Bosnia and Herzegovina, Montenegro, Bulgaria, Albania.

New target markets: Republic of Kosovo, Macedonia.

Company Profile

The company Poslovni sistem Mercator, d.d., is the controlling company of a group of associated companies (the Mercator Group), one of the largest corporate groups in Slovenia and the entire region of Southeastern Europe.

Full name	Poslovni sistem Mercator, d.d.
Abbreviated name	Mercator, d.d.
Activity	G 47.110 Retail in non-specialized food retail outlets
Identification number	5300231
VAT Tax Code	45884595
Court registry date	January 1 st 1990
Company share capital as at December 31 th 2009	EUR 157,128,514.53
Number of shares issued and paid-up as at December 31 th 2009	3,765,361
Share listing	Ljubljana Stock Exchange (Ljubljanska borza, d.d.) official market, prime market, trading code MELR
President of the Management Board & CEO	Žiga Debeljak
Management Board Members	Vera Aljančič Falež, Mateja Jesenek, Peter Zavrl
President of the Supervisory Board	Robert Šega
Deputy chairman of the Supervisory Board	Jadranka Dakič

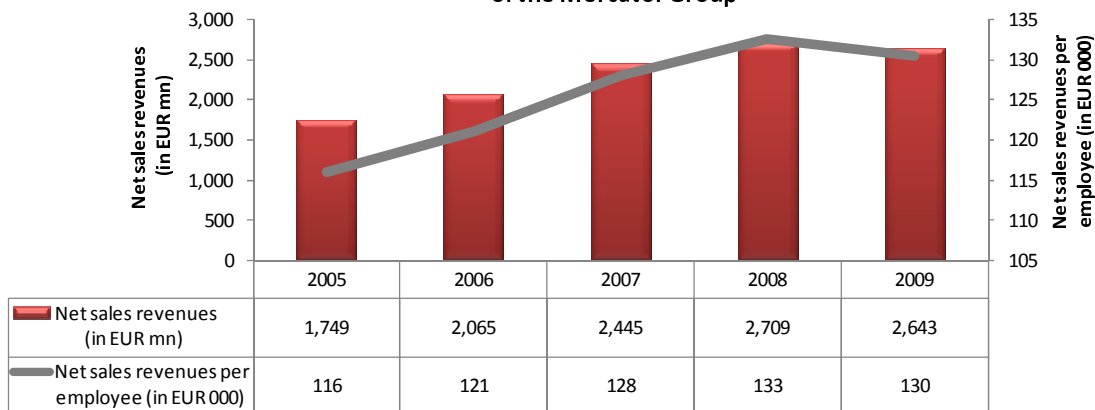
Mercator Group Activities

The most important and extensive business of the Mercator Group is **retail and wholesale** of fast-moving consumer goods (market program).

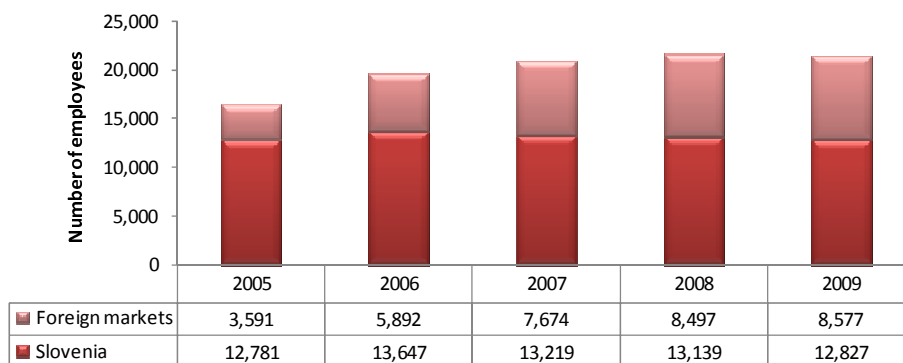
- ▶ Widely spread retail network with various store formats:
 - ▶ **market program:** hypermarkets, supermarkets, neighborhood stores, comfort stores, Hura! discount stores, and web store;
 - ▶ **specialized programs:** technical and furniture program, clothing program and drugstores, and sportswear stores.
- ▶ Numerous mutually complementing services aimed at satisfying the needs, wishes, and expectations of all our customers.

Mercator Group Development Indicators for the Period 2005 - 2009

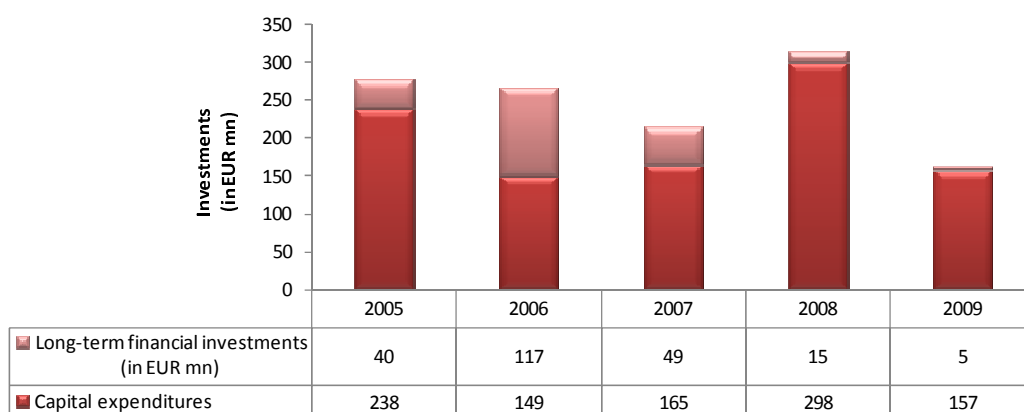
Net sales revenues and productivity of the Mercator Group



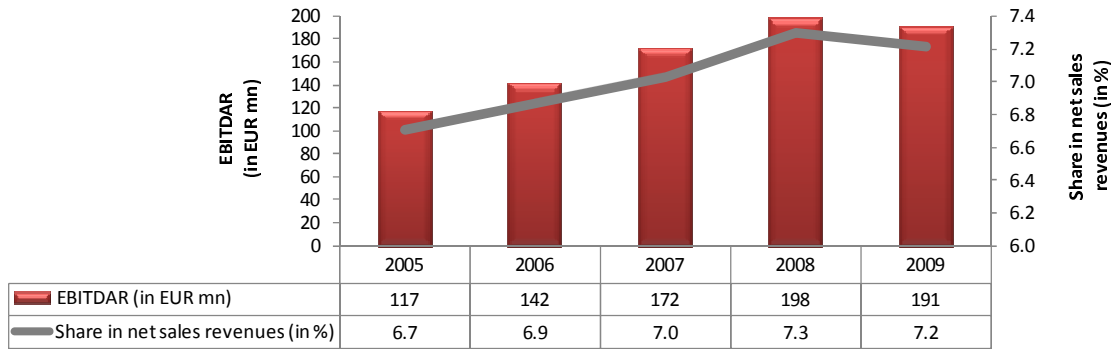
Employees



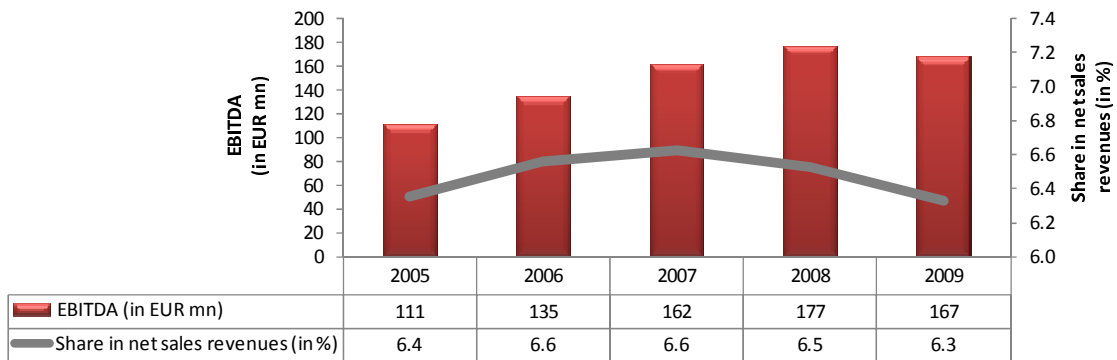
Capital expenditure and long-term financial investment of the Mercator Group



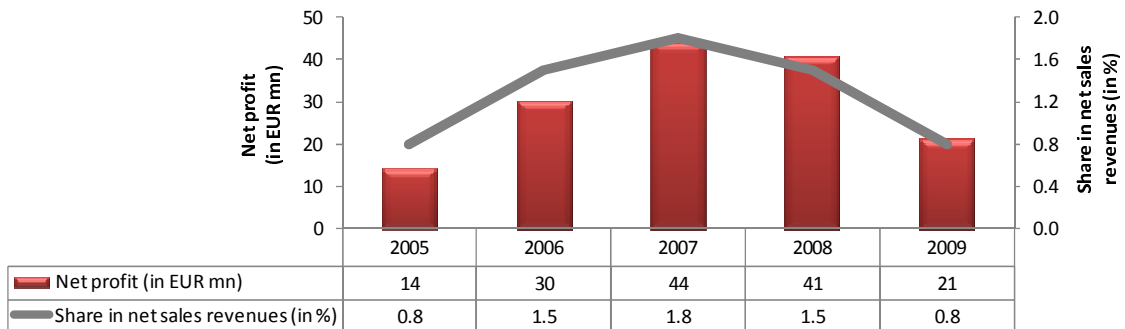
**Gross cash flow from operating activities before rental expenses
and share in net revenues of Mercator Group**



**Gross cash flow from operating activities and share
in net revenues of Mercator Group**



**Net profit and share in net revenues
of Mercator Group**



KEY EVENTS

Major Events in 2009

RETAIL NETWORK DEVELOPMENT AND ENTRIES INTO NEW MARKETS

In **Slovenia**, we opened a hypermarket and Intersport store in Škofja Loka, a hardware, electronics, and construction store in Slovenska Bistrica, a Planina supermarket in Kranj, a superette in Primskovo in Kranj, a supermarket in Preddvor, and a supermarket in Pesnica.

Openings **abroad** include the following:

- ▶ in Serbia: Roda Center Šabac, Roda Center Senta, Roda Center Sombor, a supermarket in Ruma, seven superettes and a supermarket in Sombor, four superettes in Novi Sad, a superette in Zrenjanin, a supermarket in Belgrade, and a superette in Bačka Topola;
- ▶ in Croatia: Mercator Center Varaždin, a hypermarket and Intersport store in Zaprešić, a supermarket in Buje, and a supermarket in Zagreb;
- ▶ in Bosnia and Herzegovina: hypermarket, Intersport store, Modiana, and Beautique store in the shopping center Ilidža – Sarajevo, Mercator Center Banja Luka, a supermarket in Vogošća, and a supermarket in Mostar;
- ▶ in Montenegro: a hypermarket in Podgorica.

In 2009, Mercator entered two new markets. These entries included the following openings:

- ▶ **in Bulgaria**: a hypermarket in Stara Zagora.
- ▶ **in Albania**: a hypermarket and an Intersport store in Tirana.

In 2009, a total of 95,696 square meter of gross sales area were activated.

STRATEGIC COMBINATIONS AND ALLIANCES

- ▶ On December 18th 2009, the companies Getro, d.d., and Mercator - H, d.o.o., signed an agreement on strategic alliance, pursuant to which Mercator - H will take over the trade activities of the company Getro in the market of the Republic of Croatia. The strategic alliance includes the purchase of the "Getro" brand and long-term operating lease of 16 Getro trade centers and other business facilities with a total area of over 110,000 square meter.

MARKETING AND CORPORATE ACTIVITIES

- ▶ In 2009, Mercator celebrated its **60th anniversary**. Accounting for the current economic conditions, the festivities avoided any lavishness: traditional and regular corporate events were extended, and an event was organized for Mercator Group key employees, which also hosted the president of the Republic of Slovenia.
- ▶ In 2009, we also celebrated the **10th anniversary of the Mercator brand**, as well as the **10th anniversary of the Mercator Pika card**.

- ▶ In 2009, we pursued the establishment and development of **Mercator call center** in Slovenia and set up Mercator call centers in Serbia, Croatia, and Bosnia and Herzegovina. The customers throughout the region thus have the option to call a toll-free number to obtain all information on Mercator Pika card transactions, Mercator outlets, working hours, products, campaigns, and events at Mercator stores and shopping centers. The call centers also accept customers' opinions, propositions, and praises.
- ▶ In February, we carried out our traditional meeting with our business partners – the **10th Days of Marketing**. The event that took place in Cankarjev dom was attended by a record number of 464 suppliers and other business partners.



- ▶ In March 2009, we held the **9th Financial Partners Meeting**. Held in Cankarjev Dom, the event hosted representatives of commercial banks, leasing companies, and insurance companies to inform them of Mercator Group's business plans, performance, and financial policy for 2009.
- ▶ In May 2009, the first products of the **revamped Lumpi line** were launched in Mercator stores. The assortment of products is certified by the Pediatric Clinic in Ljubljana, and the Kranj Institute of Public Health. The Lumpi logo underwent a face lift and the entire line is now distinctive for its new lovable characters called Luki, Uma, Miki, Pia, and Iki. In August, we introduced the Lumpi Club, thus announcing the revision of the line and the launch of the www.lumpi.si website.
- ▶ In September 2009, Mercator received the **Trusted Brand Award**, presented based on the results of a consumer survey by the Reader's Digest Magazine. The survey is conducted by Mediana, an independent market and media research institute. The key criteria of the survey are high quality of products and positive personal experience of the consumers. 
- ▶ In September 2009, the **3rd Mercator Human Resource Day** was held in Ljubljana. The central topic of the round table, held at Cankarjev Dom, was "Health – a Common Concern of the Employees, Employers, and the Government."
- ▶ 2009 also saw further development of the network of our own tourist offices. In Slovenia, a total of 11 **M Holidays** offices are now active.

CORPORATE GOVERNANCE

- ▶ 2009 saw some **major changes in the ownership composition** of the company Mercator, d.d. Current major shareholders are listed in more detail in the section Mercator Share and Ownership Structure.
- ▶ The 15th regular Shareholders Assembly of the company Poslovni sistem Mercator, d.d., held on July 20th 2009, saw the adoption of the resolutions on the allocation of distributable profit, dividend payment, and granting discharge to the Management Board and Supervisory Board. A **new eight-member Supervisory Board** was appointed.

Members of the Supervisory Board representing capital are Stefan Vavti, Robert Šega, Jadranka Dakič, and Kristjan Verbič. The Supervisory Board members shall assume their respective terms on October 31st 2009; pursuant to the company Articles of Association and Bylaws, the term lasts four years, i.e. until October 31st 2013. The Shareholders Assembly was informed that the Council of Employees also appointed representatives of employees for the Supervisory Board, who will assume their terms simultaneously with the representatives of capital. They are Mateja Širec, Jože Cvetek, Janez Strniša, and Ivica Župetič. The company KPMG Slovenija, podjetje za revidiranje, d.o.o., Železna cesta 8a, Ljubljana, was appointed as the authorized auditing company for the year 2009.

- ▶ At its meeting held on September 21st 2009, the Management Board of the company Poslovni sistem Mercator, d.d., adopted a resolution to launch preliminary preparation proceedings for the **issuance of up to 20 percent of new company share capital**, based on approved share capital, in order to secure in a timely manner additional financial funds to fuel any strategic combinations and alliances in the field of trade, real estate, or other activities.

PROCEEDINGS AT THE COMPETITION PROTECTION OFFICE

- ▶ Completing and terminating the proceedings instituted against the companies Mercator, d.d., Spar Slovenija, d.o.o., and Engrotuš, d.d., on the grounds of allegedly concerted action between the said companies, the Competition Protection Office issued on May 7th 2009 a decision to accept the commitments proposed to the Office by the parties in the proceedings. The commitments are related to various aspects of managing relationships between retailers and suppliers of fast-moving consumer goods, and to reporting on such activities to the Office. They will be in effect for a period of five years.
- ▶ On June 26th 2009, the Competition Protection Office, completing the proceedings instituted due to alleged abuse of dominant position in the upstream market of fast-moving consumer goods, issued a decision to accept the commitments proposed by the company Mercator, d.d. The commitments are related to various aspects of managing the relations with the suppliers of fast-moving consumer goods, and to reporting on such activities to the Office. The commitments shall be in effect for a period of five years.

Thereby, both proceedings instituted by the Competition Protection Office against the company at the end of 2007, were completed.

Major Events Following the End of 2009

- ▶ As of January 1st 2010, the new macro-organizational structure of the Mercator Group has been put in effect. The key reasons for the reorganization are the need for improved local responsiveness in all markets and improved adjustment to consumer needs, improved operating efficiency, adjustment of the organizational complexity of international operations, and preparation for the option of monetization of our trade property and facilities in order to accelerate our development cycle. The new organizational structure is presented in more detail in the section Organization and Quality of Operations.
- ▶ On January 4th 2010, the company Poslovni sistem Mercator, d.d., founded the company Modiana, d.o.o. The activities of clothing program and drugstores will be transferred to the newly founded company.
- ▶ On February 17th 2010, the companies Getro, d.d., and Mercator - H, d.o.o., completed their strategic alliance based on the agreement on the acquisition of trade activities of the

Croatian trade company Getro, d.d., signed by the partners involved on December 18th 2009.

CORPORATE GOVERNANCE

Governance of the company Poslovni sistem Mercator, d.d., and the group of associated companies is based on legislation, Corporate Governance Code for Publicly Traded Companies in Slovenia, internal rules and regulations laid out in compliance with the ISO standards, and sound business practice.

The company is managed by a four-member Management Board supervised by a Supervisory Board. The company has the following bodies of governance: Shareholder's Assembly, Supervisory Board, and Management Board.

Shareholders Assembly

Shareholders Assembly is a body of governance through which the shareholders assert their rights with regard to the company affairs. As a rule, the company Management Board convenes the Shareholders Assembly of the Poslovni sistem Mercator, d.d., once per year. The convocation of the Assembly is announced in the Delo daily paper, and in the electronic information dissemination system of the Ljubljana Stock Exchange, d.d., called SEOnet, at least one month prior to the Assembly date.

For the 15th Shareholders Assembly, the company took part in the collection of proxy authorizations from minority shareholders; the process was carried out by the Pan-Slovenian Shareholders' Association.

In 2009, 15th regular Shareholders Assembly took place with 67.28 percent of total shares with voting rights present. The Securities Market Agency had issued a decision that prohibited the companies Pivovarna Laško, d.d., Pivovarna Union, d.d., and Radenska, d.d., the assertion of their voting rights. The shareholders voted in favor of the proposal on the allocation of distributable profit and dividend payment, and granted discharge to the Supervisory Board and the Management Board. Furthermore, they appointed the Supervisory Board members representing the shareholders, and they were informed which Supervisory Board members were appointed by the Council of Employees. The shareholders appointed the auditing company KPMG Slovenija, podjetje za revidiranje, d.o.o., as the company auditor for 2009.

Supervisory Board

The fundamental function of the Supervisory Board is to supervise the management of company affairs. One half of the members, representing the interests of the shareholders, are appointed by the Shareholders Assembly, while the members who represent the interests of the employees, are appointed pursuant to the Worker Participation in Management Act, by the Council of Employees.

Members of the Supervisory Board are elected for a four-year term and may be re-elected. Pursuant to the relevant legislation and the provisions of the Rules of Procedure of the

Supervisory Board, the Supervisory Board must hold a meeting at least once per quarter, and at least once in each half of the year. In the company Poslovni sistem Mercator, d.d., the Supervisory Board holds at least five regular meetings per year.

Pursuant to the provisions of the Companies Act, the Supervisory Board appointed at its 18th meeting held on November 11th 2008, the Audit Committee for the period until October 30th 2009. At the first meeting of new Supervisory Board appointed on November 19th 2009, the Audit Committee was appointed for the period until October 31st 2013.

Presentation Of The Supervisory Board Members

As at December 31st 2009, the company Supervisory Board included eight members.

Supervisory Board Members – Representatives of capital

Robert Šega, Supervisory Board Chairman

Education:

- BS and MS Electrical Engineering & Electronics

Employment:

- business consultant to the company Epakta, d.o.o., Škofja Loka

Membership in Supervisory or Management Boards of other companies:

- Supervisory Board member at Delo, d.d.

Jadranka Dakič, Deputy Chairwoman

Education:

- BA Economics

Employment:

- deputy mayor of the Municipality of Ljubljana – non-professional position
- director of the company Lanea, d.o.o., Ljubljana

Membership in Supervisory or Management Boards of other companies:

- Supervisory Board Chairwoman at Javni Holding Ljubljana, d.o.o.
- Supervisory Board Chairwoman at Termoelektrarna Toplarna Ljubljana, d.o.o.

Stefan Vavti

Education:

- MA Economics

Employment:

- executive director for private banking in Central and Eastern European countries, UniCredit Bank Austria, AG

Kristjan Verbič

Education:

- MA Sociology; professor of philosophy and sociology

Employment:

- President of the Pan Slovenian Shareholders Association

Supervisory Board Members – Representatives of Employees

Jože Cvetek

Education:

- BA Economics

Employment:

- head of financial-accounting sector at Eta, d.d.

Janez Strniša

Education:

- BA Economics

Employment:

- head of department at Mercator, d.d.

Mateja Širec

Education:

- BA Sociology

Employment:

- head of department at Mercator, d.d.

Ivica Župetić

Education:

- BA Economics

Employment:

- advisor to the executive director of international development; employed at Mercator - H, d.o.o.

Management Board

The company Poslovni sistem Mercator, d.d., is managed by the Management Board consisting of a president and three members. The president submits to the Supervisory Board a proposal for the appointment of the remaining Management Board members, and the Supervisory Board appoints the entire Management Board for a five year term, with unlimited entitlement for re-election. The number of Management Board members and their respective fields of work and responsibilities are defined as proposed by the president of the Management Board and confirmed by the Supervisory Board with the adoption of the Management Board Act. The Management Board manages company affairs independently, responsibly, and to the benefit of the company.

Supervisory Board resolution dated December 13th 2005, appoints the members of the Management Board of the company Poslovni sistem Mercator, d.d., for a five-year term, starting on January 1st 2006. All Management Board members of the company Poslovni sistem Mercator, d.d., signed their respective fixed-term employment agreements with the company Poslovni sistem Mercator, d.d., for the period of five years, which is consistent with the duration of their term.

Presentation of the Management Board members

As of January 1st 2006, the Management Board of the company Poslovni sistem Mercator, d.d., consists of the president and three members, appointed for a five-year term. Following is their brief presentation.

Management Board President - Žiga Debeljak

Education:

- MScBA, BS Computer Engineering

Fields of responsibility:

- Coordination of Management Board and Group governance
- Development and investment
- IT
- Finance, controlling, accounting, internal audit, and investor relations

Other responsibilities:

- Member of the Administrative Committee of the Manager Association
- Member of the Council of the Faculty of Economics in Ljubljana
- Member of the Council of the National Gallery

Membership in other administrative or supervisory bodies of non-associated companies:

- Supervisory Board Chairman at the company Pokojninska družba A, d.d.
- Supervisory Board member at Petrol, d.d.

Management Board member in charge of human resources, organization, legal and general affairs - Vera Aljančič Falež

Education:

- LL.M., LL.B.

Fields of responsibility:

- Human resource management
- Organization and quality
- Legal affairs
- General affairs

Other responsibilities:

- Member of the Administrative Board of the Slovenian Chamber of Commerce
- Deputy Chairwoman of the Council of the Institute of Innovation and Development of the University of Ljubljana
- Chairwoman of the Pension Plan Committee at Pokojninska družba A, d.d.
- Member of the Economic and Social Council
- Managing Board member at the Slovenian Association for Human Resource Management and Industrial Relations

Management Board member in charge of marketing and purchasing – Mateja Jesenek

Education:

- MBA, BA Economics

Fields of responsibility:

- Product and service marketing
- Market research and development
- Purchasing and supplier relations
- Public relations

Other responsibilities:

- Marketing Board member at the Consumer Goods Forum, a global association of manufacturers and retailers
- Supervisory Board member at the Slovenian Marketing Association
- Honorary chairwoman of the Society for Promotion of Women in Culture - The City of Women ("Mesto žensk")
- President of the Program Council of the 14th Slovenian Marketing Conference 2009
- Member of the UNICEF Economic Council

Management Board member in charge of retail, wholesale, and logistics –

Peter Zavrl

Education:

- BA Economics

Fields of responsibility:

- Retail,
- Wholesale,
- Franchise system
- Logistics

Other responsibilities:

- Chairman of the Krim Mercator Handball Club,
- Head of the Supervisory Committee at the Kranj Radioclub

Audit Committee

The activities of the Audit Committee are aimed at further improvement of performance of the supervisory function in the company.

The tasks of the Audit Committee include monitoring the process of financial reporting, monitoring the efficiency of internal control in the company, internal audit and risk management systems, monitoring the mandatory audit of annual and consolidated financial statements, reviewing and monitoring the independency of the auditor appointed to audit the company Annual Report, particularly in terms of providing additional non-audit services, proposing to the Supervisory Board the candidate to be appointed as the company Annual Report auditor, verifying the validity of financial information submitted by the company, appraisal of the Annual Report contents and composition, including submitting a proposal to the Supervisory Board, taking part in defining the key auditing areas, taking part in the preparation of a contract between the auditor and the company, performing other tasks defined either by Articles of Association and Bylaws or a Supervisory Board resolution, and working with the auditor during the company Annual Report audit.

The Audit Committee at the company Poslovni sistem Mercator, d.d., for the period until October 30th 2009 consisted of the president Mrs. Mateja Vidnar, (Supervisory Board member) and two members: Mr. Jože Cvetek (Supervisory Board member) and Mr. Peter Ribarič (independent expert on accounting and auditing). As of November 19th 2009, the Audit Committee consists of the president Mrs. Jadranka Dakič (Supervisory Board member) and two members: Mr. Jože Cvetek and Mr. Peter Ribarič.

Management of Subsidiaries

Mercator Group consists of the parent company Poslovni sistem Mercator, d.d., and its subsidiaries in which the parent company holds, directly or indirectly, the majority interest or the majority of voting rights. Parent company controls its subsidiaries within a single Management Board.

The company Poslovni sistem Mercator, d.d., as the parent company of the Mercator Group, operates by the principles of improving business performance in each subsidiary and the Group as a whole, common harmonized development of the Group, optimal supply of fast-moving consumer goods and services in all markets of Group's operations, improving competitiveness, efficient allocation and coordination of material flows, harmonized and coordinated procurement and sales at home and abroad, financing current operations and development with common funds, and security, risk and liquidity management, and maximum returns in financial management.

In Slovenian and foreign subsidiaries incorporated as limited companies (d.o.o.), the parent company's Management Board performs the function of company Assembly; alternatively, the parent company's Management Board, either entirely or partially (with involvement of only some of its members), takes part in the work of the Supervisory Boards of these companies. The employees present in the bodies of governance at these companies do not receive any additional compensation for performance of such functions.

Audit

In today's continuously changing environment, efficient and successful business operation requires accurate and prompt information. Whilst the management of the company is responsible for providing relevant financial information, the paramount task of internal and external audit is to minimize the risks related to the preparation as far as possible.

Internal auditing

The independent support function of internal audit has been introduced in the Mercator Group in the year 2000; since, it has been actively performed both within the parent company and at the Group level. Basic function of internal audit is perpetual development and monitoring of the internal control systems from the aspect of managing, or hedging, all sorts of operating and other risks to which the Mercator Group is exposed.

Internal audit includes regular and extraordinary auditing of particular areas of operations of the Mercator Group companies, as well as collaboration with external auditors. In 2009, regular audits included a review of the implemented measures and financial effects of the Mercator Group Operations Optimization Project, and monitored the implementation of cost rationalization measures at the Mercator Group. Internal audit of the non-trade goods and services within the SAP IT system was repeated. Furthermore, internal audits of the data warehouse at Mercator, d.d., of the entire process of the Mercator Pika card at the company Mercator, d.d., and of the measures for managing key risks at the Mercator Group, were also carried out.

External auditing

External auditing is carried out by a certified auditing company which, in addition to regular annual audit of the company's financial statements, also provides expert consulting including warnings and proposals for the improvement of the internal control systems for successful management of all types of risks.

Pursuant to the resolution adopted at the 15th regular Shareholders Assembly of the company Poslovni sistem Mercator, d.d., auditing company KPMG Slovenija, podjetje za revidiranje, d.o.o., was appointed as the external auditor for the year 2009 as well.

Communication with Shareholders and Reporting

The strategy of communicating with the shareholders, financial analysts and institutions, the media, and the general public, is based on the pursuit of transparency and clarity of our operations; this is achieved at Mercator by regular and timely announcement of information on the company status, as well as on major changes in company operations.

A considerable part of communication with the financial community takes place through announcements on the Ljubljana Stock Exchange website, within the SEOnet, the electronic information dissemination system, where we have been publishing all announcements simultaneously in Slovenian and English since 2005, and where all financial statements and reports for the company and the Group have since been published in compliance with the International Financial Reporting Standards.

In 2009, we held regular meetings with various members of the financial community. We also took part in the Days of Slovenian Capital organized by the Ljubljana Stock Exchange and the Central Securities Clearing Corporation in Ljubljana. At the event, Mercator Group was presented to various domestic and international portfolio issuing authorities. In March 2009, we met with our financial partners for the ninth consecutive year. We presented them the Mercator Group development policies for 2009, business performance in 2008, and the Group financial policy for 2009. We also took part in promotions organized by representatives of the capital market.

BUSINESS STRATEGY OF THE MERCATOR GROUP

Strategic policies and strategic goals of the Mercator Group for the medium term period 2008 - 2012 were adopted in December 2007. A summary thereof was published on December 18th 2007 on SEOnet, the electronic information dissemination system of the Ljubljana Stock Exchange, d.d.

Vision

To be the leading retail chain with FMCG program (market program) in Southeastern Europe.

Mission

Our business is aimed at creating:

- ▶ benefit for the customers by providing excellent retail services, high-quality goods and competitive prices,
- ▶ benefit for employees by providing a safe and pleasant working environment and a possibility of personal and professional development,
- ▶ benefit for suppliers by taking part in the development of high-quality and innovative products and by providing the possibilities for growth in Slovenia and in emerging markets,
- ▶ benefit for shareholders by attaining a profitable growth of business operations, improving business efficiency, and increasing the company market value,
- ▶ benefit for wider environment by a responsible attitude towards our natural and social environment and by respecting the business ethics and social values in all fields of operation.

Corporate culture values

We are bound by trust and mutual respect. Our values are:

- ▶ sound teamwork,
- ▶ sincere relationships,
- ▶ encouraging creativity,
- ▶ motivating the fellow workers.

Nobody knows the customer preferences better than we do. Our values are:

- ▶ unwavering education at home and abroad,
- ▶ constant transfer of knowledge,
- ▶ ensuring personal growth and development,
- ▶ excellent staff competitiveness.

Our operations are always diligent and transparent at all levels. Our values are:

- ▶ competitiveness as the foundation of any partnership,
- ▶ accessibility of key information,
- ▶ consistency and honesty.

We are expanding with a sound corporate culture. Our values are:

- ▶ training key human resources for assuming international tasks,
- ▶ understanding the differences and adapting to local environment.

Strategic policies

1. LARGEST RETAILER IN SLOVENIA - To retain the leading market share of market program in Slovenia, primarily by the following activities:
 - ▶ improving the competitiveness of our offer,
 - ▶ developing the retail network.
2. LEADING RETAILER ON NEIGHBORING MARKETS OF SE EUROPE - To become the largest or second largest retailer with market program in the markets of Croatia, Serbia, and Bosnia and Herzegovina, by:
 - ▶ strategic combinations and alliances,
 - ▶ development of our own retail network.
3. ENTERING OTHER SE EUROPEAN MARKETS - To enter or enable the entrance to other markets in Southeastern Europe, where we could become one of the five leading retailers with market program; this will be attained by:
 - ▶ purchasing attractive locations,
 - ▶ development of our own retail network,
 - ▶ strategic combinations and alliances.
4. DEVELOPMENT OF NON-MARKET PROGRAMS - To develop non-market programs and supplementary programs that will:
 - ▶ enable reaping the potential of positive synergies with market program and/or
 - ▶ provide a concept for development of the second fundamental commercial program with a long-term potential of growth and profitability in the target markets,
 - ▶ foster the development of long-term competitive advantages.
5. PROFITABLE OPERATION - Ensure profitable operation by:
 - ▶ measures for retaining the level of trade margins,
 - ▶ measures for cost rationalization and increasing the productivity,
 - ▶ measures for increasing the productivity of invested capital.

ECONOMIC CONDITIONS IN 2009

Business environment in 2009 was extremely challenging due to negative economic growth, credit crunch, and other effects of the global financial crisis. The level of economic activity was considerably lower than expected in all markets, which was in turn reflected in the changes of the volume and composition of consumer demand. In addition, nominal financing costs remained relatively high due to the effects of the global financial crisis, despite falling reference interest rate.

Macroeconomic position of numerous countries in the Western Balkans is troubled and the payment indiscipline, resulting from the restricted amount of credit available to enterprises and individuals, is posing another notable risk. Furthermore, the Republic of Serbia has seen considerable depreciation of its local currency whose average EURO exchange rate rose by

15.6 percent in 2009 compared to the year before. Another notable effect on Mercator's operations was a result of the drop in real purchasing power of the consumers in these countries.

In order to cope with the effective economic conditions, the Management Board of the Mercator Group has introduced two sets of measures:

- ▶ **Adjusting the offer for the consumers**, effected by:
 1. adjusting the sales assortment;
 2. price competitiveness;
 3. customer loyalty system upgrade.
- ▶ **Operating rationalization**, effected by:
 1. cost rationalization;
 2. restriction of investment volume;
 3. efficient risk management.

▶ **Slovenia**

According to first estimates, Slovenia's economy has shrunk by 7.3 percent in 2009, which is a notable drop in the rate of economic growth compared to 2008 (+3.5 percent). The decline of growth was brought about primarily by the collapse of international trade as Slovenia's GDP is significantly export-dependent.

▶ **Croatia**

The first estimates for 2009 indicate a 6 percent decline in the Croatian economy in 2009. The shrinking of the economy is a result of a considerable fall in household consumption. In December 2009, year-on-year inflation amounted to 1.9 percent. Average annual exchange rate for Croatian kuna in 2009 amounted to HRK 7.34 per 1 EUR (HRK 7.22 per 1 EUR in 2008). As at December 31st 2009, the closing rate was HRK 7.30 per 1 EUR.

▶ **Serbia**

According to first estimates, economic growth in Serbia was negative in 2009, at 2.9 percent. The prime reason for the GDP drop was a decline in the processing industry, trade, and construction. Average annual exchange rate for Serbian dinar in 2009 amounted to RSD 93.79 per 1 EUR, which is 15.6 percent more than the average rate in 2008. As at December 31st 2009, the rate was RSD 95.03 per 1 EUR, which is 6.3 percent more than on December 31st 2008.

▶ **Bosnia and Herzegovina**

The first estimates for Bosnia and Herzegovina in 2009 also indicate a negative economic growth at 3.0 percent. The recession is expected to extend into 2010 as domestic demand is expected to remain weak, fiscal policy austere, and unemployment higher. Exchange rate of the Convertible marks is pegged to the euro at the rate of BAM 1.95583 per 1 EUR.

▶ **Montenegro**

Lower domestic and foreign demand is estimated to result in a 4.0 percent drop in the Montenegrin economy in 2009. The currency used in Montenegro is EUR.

▶ Bulgaria

According to first estimates, Bulgaria saw a 6.3 drop in the economic growth in 2009. The main reason for the slump was the decline in both exports and domestic demand, resulting mostly from the lower investment and household consumption. Exchange rate for the Bulgarian lev is pegged to the euro at the rate of BGN 1.9558 per 1 EUR.

▶ Albania

The first estimates by the Albanian government indicate a 4.0 percent economic growth in this country in 2009, making it one of the very few countries whose modest integration into the international monetary flows allowed a positive GDP growth in 2009. Average annual exchange rate for the Albanian lek amounted to ALL 131.55 per 1 EUR in 2009. As at December 31st 2009, the closing rate was ALL 138.90 per 1 EUR.

DEVELOPMENT AND INVESTMENTS

In 2009, Mercator Group's investment into property, plant, and equipment amounted to EUR 157,353 thousand, of which EUR 108,520 (69.0 percent) was invested abroad. The majority of funds, amounting to EUR 108,831 thousand, or 69.2 percent, were allocated for construction, acquisition, completion, and furnishing of shopping centers or landed property. Remaining funds were invested in new individual stores, refurbishments, distribution centers, and IT.

Investment breakdown

Country	Capital expenditure 1-12 2009 (in EUR 000)	Structure in %
Slovenia	48,833	31.0%
Serbia	49,970	31.8%
Croatia	24,882	15.8%
Bosnia and Herzegovina	16,967	10.8%
Montenegro	4,059	2.6%
Bulgaria	6,376	4.0%
Albania	4,986	3.2%
Macedonia	1,280	0.8%
TOTAL	157,353	100.0%

▶ SLOVENIA

▶ On April 30th 2009, we opened a **hypermarket and Intersport** in **Škofja Loka**, including one supplementary service outlet (a café). The newly built facility extends over a total area of 3,516 square meter and it includes 113 parking spots.



▶ On December 10th 2009, we opened a **Hardware, electronics, and construction center** in **Slovenska Bistrica**. The facility has a total area of 1,903 square meter.

▶ **Other openings:** supermarket Planina in Kranj with a total area of 784 square meter, on February 5th 2009; extended and refurbished superette in Primskovo, Kranj, on May 23rd 2009; supermarket in Preddvor on November 27th 2009; supermarket in Pesnica on December 1st 2009.

FOREIGN MARKETS

▶ CROATIA

▶ On May 21st 2009, **Mercator Center Varaždin** was opened, extending over a total area of 9,310 square meter and including 411 parking spots, of which 266 are located in the basement garage. The program mix is offered in a hypermarket (total area of 3,037 square meter), Intersport, Modiana, café, and 21 outlets offering supplementary services.



▶ On November 12th 2009, **hypermarket and Intersport** were opened in the West Gate Shopping City in **Zaprešić** near Zagreb. The hypermarket has a total area of 7,444 square meter; that of the Intersport amounts to 2,437 square meter. Both outlets are leased.



▶ **Other openings:** supermarket in Buje on March 4th 2009 and superette Odra in Zagreb on October 15th 2009.

▶ SERBIA

▶ On February 25th 2009, we opened **Roda Center Šabac**, a facility with a total area of 14,646 square meter and 206 parking spots, of which 180 are roofed. The center includes a hypermarket with a total area of 4,379 square meter, Intersport, Modiana, Beautique, hardware and electronics store, and 39 outlets offering supplementary services. The center is subject to a long-term lease agreement signed by the company Mercator - S, d.o.o.



▶ On December 17th 2009, **Roda Center Senta** was opened. The facility has a total area of 3,268 square meter and 62 parking spots of which 52 are in a garage. In addition to the supermarket with a total area of 1,706 square meter, the center also includes 19 outlets leased to third-party providers of supplementary services.

▶ December 18th 2009 saw the opening of **Roda Center Sombor**, a facility with a total area of 5,390 square meter and 45 parking spots in a garage. The center includes a supermarket with a total area of 1,290 square meter, Intersport, Modiana, Beautique, hardware store, and 10 outlets offering supplementary services. The center is subject to a long-term lease agreement signed by the company Mercator - S, d.o.o.



▶ **Other openings:** On April 28th 2009, we opened a supermarket in Ruma; in the course of 2009, seven additional superettes and a supermarket were opened in Sombor (lease of the outlets of the food retail chain Prehrana, a.d.); four superettes in Novi Sad (lease of the Centroslavija outlets); a superette in Zrenjanin; supermarket Konjarnik in Belgrade; and a superette in Bačka Topola.

▶ BOSNIA AND HERZEGOVINA

▶ On April 16th 2009, we opened a **hypermarket, Intersport, Modiana, and Beautique** in the **Ilidža – Sarajevo** shopping center. Total area of the leased and fully furnished Mercator outlets amounts to 3,643 square meter, of which hypermarket extends over 2,690 square meter.



▶ On May 7th 2009, **Mercator Center Banja Luka** was opened. The facility has a gross area of 17,271 square meter, and a garage with 631 parking spots. The center includes a hypermarket (total area of 6,201 square meter), Intersport, Modiana, Beautique, and 51 outlets leased to third party service providers.



▶ **Other openings:** On December 10th 2009, Hayat supermarket was opened in Vogošća; on December 23rd 2009, supermarket Carinski most was opened in Mostar. Both outlets are subject to a long-term lease.

▶ MONTENEGRO

▶ On December 12th 2009, we opened a **hypermarket** in the Mall of Montenegro **in Podgorica**; the hypermarket has a total area of 4,349 square meter. An Intersport store is scheduled for opening in the same mall for March 2010.



▶ BULGARIA

▶ On October 7th 2009, the opening of a 3,002 square meter **hypermarket in Stara Zagora** marked our entry into a new market – Bulgaria.



▶ ALBANIA

▶ On December 19th 2009, the opening of a **hypermarket and an Intersport store** in City Park shopping center **in Tirana** marked our entry into a new market – Albania. The two facilities extend over an area of 4,494 and 1,022 square meter.

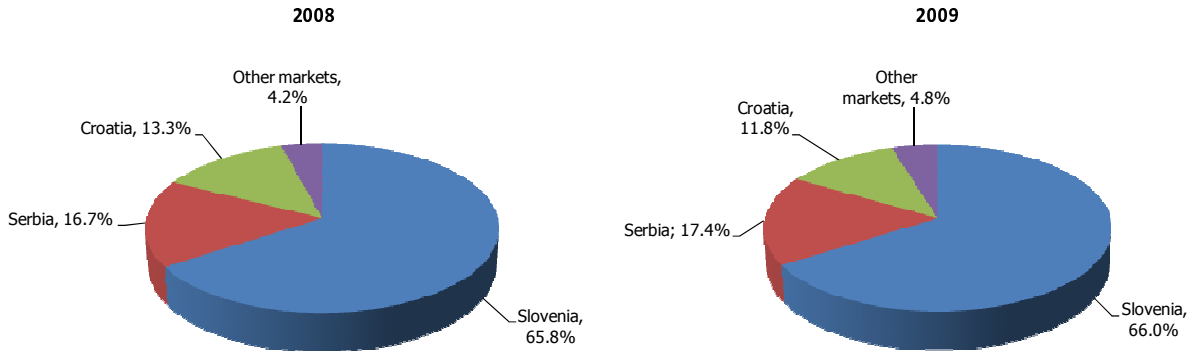


SALES AND MARKETING

Sales

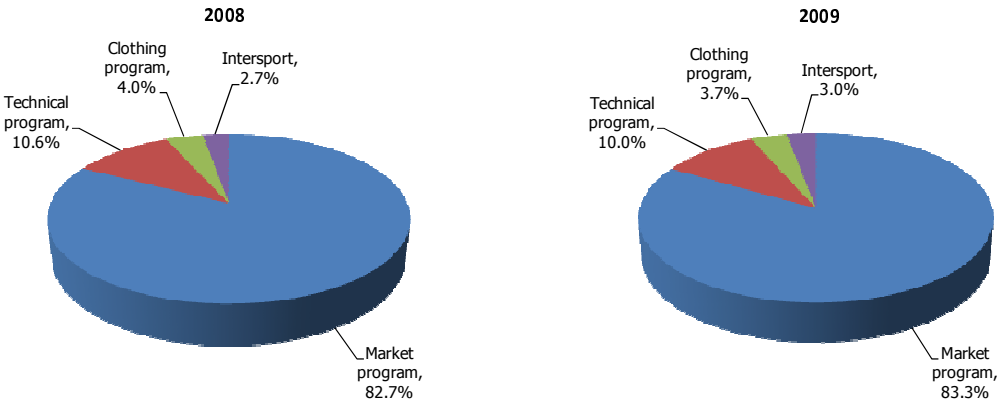
In 2009, Mercator Group generated a total of EUR 2,643 million of net sales revenues, which is 2.4 percent less than in 2008. Assuming constant exchange rates, net revenues from sales would have amounted to EUR 2,724 million, topping the 2008 figure by 0.6 percent.

Mercator Group net sales revenues by geographical segments:



In Slovenia, Mercator Group net sales revenues amounted to EUR 1,745 million in 2009, which is 2.1 percent less than in 2008. In foreign markets, EUR 899 million of net sales revenues was generated in 2009, which is 3.0 percent less than in the year before. Assuming constant exchange rates, revenues abroad would have amounted to EUR 979 million, exceeding the 2008 figure by 5.7 percent.

Mercator Group net sales revenues by programs:



In 2009, the majority of Mercator Group trade revenues resulted from sales of market program products as they accounted for 83.3 percent of total net sales revenues; revenues from other specialized programs amounted to 16.7 percent.

Category Management

In 2009, category management in Slovenia was focused on improving the price competitiveness and perception in Slovenia. To this end, a pricing model was developed based on the price elasticity of each product, and other relevant economic criteria. Simultaneously, we launched the development of a promotional tool through simulation of marketing mix effects (product, price, promotion, place); the aim of this tool is to improve the effectiveness of our promotions. At the end of the year, we also started to develop an assortment model that will allow defining the assortment in each store according to the store format and the presence of a particular category.

In 2009, we refreshed the planograms for the majority of categories at all hypermarkets, in order to improve our sales results, to optimize the profit margin, and to improve inventory

turnover. At the same time, we conducted the preparation for further expansion of planograms to major supermarkets.

In Croatia, we set up market program organization in compliance with the principles of category management, and established a reporting system. In the second half of the year, we focused on improving price competitiveness and price perception, and on developing the strategies of select categories.

Marketing Strategy and Market Share

By offering added value for the customer and providing a pleasant modern shopping experience, we wish to elevate Mercator to the position of the most competitive retailer in the market.

- ▶ Our customers will be offered services and products fitting today's modern way of life;
- ▶ We shall promote environmental responsibility and care for health;
- ▶ We shall have an innovative offer of products and services.

Changed social and economic conditions provided the guideline for our marketing and purchasing activities, as well as for the definition of our priorities, which include the following:

- ▶ Customer care and adjustment to the new market conditions: intensive adjustment of prices of the most commonly sold products;
- ▶ Upgrade of the Mercator Pika card customer loyalty system;
- ▶ Development of private label line products;
- ▶ Adjustment of the sales assortment and sales area;
- ▶ Rationalization of marketing activities, but not at the expense of the customer benefits;
- ▶ High level of service;
- ▶ Social accountability.

Market Share

Mercator Group market shares in particular FMCG markets in 2009 are estimated as follows:

	Slovenia	Serbia	Croatia	Bosnia and Herzegovina	Montenegro
Market share	35-36 %	8-9 %	5-6 %	4-5 %	4-5 %

Source: Mercator estimates.

Due to notable changes in the volume and composition of consumption, resulting from the economic crisis, no reliable measurements of market shares are available for 2009. Mercator prepared these estimates based on in-house analyses and other available sources; market shares are estimated in intervals.

Changes in Consumer Behavior and Effect of the Crisis on Consumption

The economic crisis has extended over the entire year 2009, weakening the purchasing power of the population. As the consumers are concerned about their financial status, they respond to the crisis by changing their consumption patterns and habits. Economic situation remains among the major worries of modern consumers who tend to control their spending more strictly, deciding on replacement purchases only when it is really necessary, and often opting for D.I.Y. ("Do It Yourself") rather than hiring costly services. When shopping, they pay closer attention to the price, and the purchases are more planned and thought out as the customers are seeking the best ratio of value for money.¹

The global trends reflected in some of Mercator's target markets and affecting the consumption during recession could be summarized as follows:

- ▶ The existing hierarchy of values has been shattered; consumers are much more price-aware which incites a shift towards more affordable products and private label products.
- ▶ Shopping is more rational and thought out, there is less impulse buying and less experimentation with previously unfamiliar products and innovations.
- ▶ Major purchases are postponed.
- ▶ The consumers increase their savings rate.
- ▶ Leisure time activities are changed, leading to a different lifestyle (eating out is less common; consumers prefer preparing their meals at home).
- ▶ Frequency of shopping trips: the consumers go shopping less often; when they do, the average basket is larger.
- ▶ Consumers are changing their shopping destinations: more shopping is done in discount stores.
- ▶ There is a shift in the importance of care for health and the environment.
- ▶ Increased use of the worldwide web, social networks, and technologies where "the information finds the user" or where the user generates the information, and which allow direct interaction between the company and the user.

According to the information provided by the Slovenian Marketing Association and the Valicon market research agency, Slovenian users most drastically reduced their expenditures for furniture and accommodation (55 percent of all consumers), major purchases and investments (54 percent of all consumers), clothing and footwear (52 percent of all consumers), tourist services (50 percent of all consumers), and consumer electronics and home appliances (49 and 47 percent of all consumers, respectively). 26 percent of all consumers have reduced their expenditures for alimentary products or fast-moving consumer goods.²

Economic crisis affected the shopping habits both in Slovenia and in Mercator's foreign target markets. According to the Shopper Trends 2009 research,³ consumers respond to the crisis by purchasing lesser quantities of the same products, by actively seeking special offers, making use of the customer loyalty and benefit programs, and turning to private label products. The crisis also struck the Eastern European countries where the consumers mostly

¹ Source: Consumer Insights / MGI Europe survey, McKinsey Global Institute EU Consumer Team analysis

² Source: Slovenian Marketing Association and Valicon, April 2009

³ Source: ACNielsen 2009

restrict their shopping to basic products and often look in several different stores to find the best prices.

In the second half of 2009, the decline in consumption was slightly mitigated. Although the consumers remain modest in their spending, they entered 2010 with more optimism than displayed in 2009.

Mercator's Response to the Changes in the Economic Environment

Mercator responded to these changes with numerous campaigns and activities. Perhaps the most notable among them is the campaign **"we cut the prices of 2,800 products"** which started in February 2009 and continued throughout the year. The project was also set up in Croatia.



Responding to the rational behavior of the consumers, we also **expanded the generic line of our private label**. Related communication took place in April and already positive response to the campaign is perceivable as generic products have become the best-selling products in some categories.



Customers from the more threatened groups (pensioners, working class) are offered special discounts. As of September 2009, **members of the Slovenian Association of Free Trade Unions** are offered the following benefits when paying with the ZSSS-DH benefit card: 2 percent discount on the entire value of the purchase at all Mercator stores, eligibility for Special Pika Discounts under the same conditions as applicable to the Mercator Pika card holders, and 10 percent discount on the basket of 20 products, which is updated every three months.

Customer Relations Management

10 Years of Mercator Pika Card Activities

Ten years of Mercator Pika card activities is a result of a solid and long-lasting partnership relation between Mercator and its customers. **Even during recession, the share of retail revenues generated by Mercator Pika card purchases is rising.** Mercator Pika card, due to being a credit card and offering benefits of Special Pika Discounts, as well as those provided through the network of our partner companies, has spread among the majority of active population in Slovenia, thus becoming a major asset of Mercator both in the highly competitive retail industry and in the segment of credit and debit cards.

Mercator Pika card Customer Loyalty System

At the end of 2009, there is a total of **1,433,799 Mercator Pika card holders** in **four markets of our operations**.

Mercator Pika card holders	Slovenia	Serbia	Croatia	Bosnia and Herzegovina	Total
As at Dec 31 st 2008	836,851	129,017	213,418	92,551	1,271,837
As at Dec 31st 2009	917,499	154,915	243,329	118,056	1,433,799
New holders in 2009	80,648	25,898	29,911	25,505	161,962

In Slovenia, the **share of total retail revenues generated by purchases completed with Mercator Pika card** amounted to **54.6 percent** in 2009 (50.8 percent in 2008). In all markets of **Mercator operations** combined, this share amounted to **44.1 percent** (40.6 percent in 2008).

In cooperation with our partners in the Mercator Pika card system, we prepared the **Special Pika Discount** campaign each month. Two new partners were added to the Mercator Pika card customer loyalty system: **Kaval Group** and **Lipica Turizem**. To celebrate the **10th birthday** of the Mercator Pika system, a major prize competition was organized for all Mercator Pika card holders who responded to our collection of permissions for direct and targeted marketing.



Revision of the Mercator Pika Card Customer Loyalty System

In addition to all basic advantages of the previously existing system, the new system delivers simplification of procedures, cost rationalization, higher level of services, and new possibilities for customer loyalty system upgrade which would allow adjusting the offer to the target segments.

Maxi Club

The purpose of the Maxi Club is to provide a link between people who like shopping in the tranquil environment of the Maxi department store and who value the high quality of offer and expert service. At the end of 2009, Maxi club has a membership of 11 thousand.

M Mobil

By launching the M Mobil service in 2006, Mercator became the first retailer in Slovenia to enter the mobile telephony market. Club members, also Mercator Pika card holders, are included in the M mobil benefit and bonus system.

Healthy Lifestyle Club

In June 2009, the Healthy Lifestyle Club celebrated its 3rd anniversary. The club is intended for people of all generations who share the idea of a healthy lifestyle and who are seeking more information on wholesome nutrition, exercise, and quality leisure time. At the end of 2009, the club had a membership of 61 thousand.

Lumpi Club

In May 2009, we founded the Lumpi Club to offer sage advice on upbringing, nutrition, care, education, play, and development of children. Advice is prepared in cooperation with renowned experts, while parents can share their personal experience. The website regularly informs the club members of club activities, events, and workshops for the children. The members are also offered discounts on products and services. At the end of 2009, Lumpi Club had 14 thousand members.



M Holidays

In 2009, we continued to offer under the M Holidays brand our tourist arrangements. We also extended the network of our own tourist offices: eleven were newly opened in 2009. The offer of tourist arrangements are presented in Mercator special offer flyers and on our website found at www.mholidays.si.

Mercator Call Center

In 2009, Slovenian call center was joined by call centers in Serbia, Croatia, and Bosnia and Herzegovina. Operators of the call centers are available at toll-free numbers 24 hours a day, every day of the year, ready to provide customers and Mercator Pika card holders with information and answers to their questions. Thus far, over 400,000 calls were accepted in the entire region (Slovenia, Serbia, Croatia, and Bosnia and Herzegovina).

Mercator Web Store

In 2009, we carried on our activities to prepare for the comprehensive upgrade of the Mercator web store offer. Despite the crisis, revenues generated by the Mercator web store have not declined in 2009.

Mercator Web Portal

The web traffic at Mercator websites is growing each year: in 2009, it rose by nearly 40 percent compared to the year before. In addition to setting up the employment portal intended for both those seeking employment and current employees, we set up web presentations in Mercator's new markets, Bulgaria and Albania.

Mercator at Social Networking Sites

In 2009, we have devised our strategy for presence at social networking sites and set up our profiles. Mercator (www.facebook.com/Mercator) and Lumpi (www.facebook.com/LUMPI) profiles were set up on Facebook, and a prize competition was organized. On Twitter, we set up an account @mercator_sl. Two channels were opened on YouTube, one for Mercator and the other one for the Lumpi brand. We also have a presentation page on LinkedIn and Wikipedia.

Customer Satisfaction Survey

Each year, we conduct a customer satisfaction survey in each market of our operations; the surveys include customers of all store formats. The objective of the research is to identify any gaps between the level of customer satisfaction and the level of importance of particular elements of service and offer. Based on these findings, improvement proposals are made. Total average satisfaction rating for 2009 was **4.2** (on a scale from 1 to 5), which remains the same as last year.

Perception of Quality and Pricing

Mercator is regularly monitoring the perception of quality and pricing among its customers. Mercator has the reputation of the retailer offering the highest quality of products, as well as a trustworthy retailer offering the customers the best quality for the price paid.

Operations in the Markets of Southeastern Europe

In **Serbia**, the number of Mercator Pika card holders rose sharply in 2009, with the green card taking the highest share. In order to increase the number of card users, we have carried out in-store promotion activities and regularly informed the customers on novelties and benefits offered by the Mercator Pika card.

Customer relations management activities in **Bulgaria** in 2009 included a research on the attitude towards retail chains, and a research on current attitude to Mercator Stara Zagora among the current and potential customers.

In **Bosnia and Herzegovina**, we organized a competition among the cashiers / checkout assistants in signing new Mercator Pika card holders, rewarding those most successful. We also carried out several other activities to attract new Mercator Pika card holders.

In **Croatia**, various campaigns were carried out: Pika Day, Special Pika Discounts, Pika's Happy Week, double and triple Pika points, category discounts, and other campaigns. The checkout assistant competition in signing new Pika members took place in Croatia as well, and the most successful checkout assistants were rewarded.

Development of Private Label Lines and Exclusive Brands

In 2009, we continued to pursue our goals in the field of private label line and exclusive brand development. These goals include the following:

- ▶ preparing the strategies for development and future upgrade of Mercator private label lines and exclusive brands;
- ▶ improving the reputation and distinctiveness of the private label lines;
- ▶ motivating purchases by various target groups of consumers through sales promotion activities and innovative communication;
- ▶ growth of the share of private label products in total sales revenues and increasing the number of products offered under private label lines;
- ▶ developing new products by emphasizing safety and quality of products of all private label lines (in-house product testing and external testing at the Faculty of Biotechnology and the Institute of Public Health Kranj);
- ▶ launching the revised Lumpi line;
- ▶ new development concept for the cosmetics and body care products within the exclusive Trebnik Mansion ("Dvorec Trebnik") line.

Private label and exclusive brands include the following product lines:

▶ **Mercator Line** includes alimentary products, products for households, and products of textile and hardware and electronics program. It seeks to offer the best price to quality ratio. To celebrate the 10th anniversary of the Mercator private label, we prepared special "gratis" product packages and a private label promotion flyer, and intensified our advertising efforts for special offers in the media.

▶ **Trebnik Mansion** ("Dvorec Trebnik") is a new exclusive line of high-quality cosmetics and body and facial care products. The products contain natural ingredients, and a selection of scents, fragrances, and other ingredients attuned to the most recent market trends.



▶ **Grosuplje Bakery** line includes premium bread and pastry.

▶ **Ambient Line** includes high-quality products for interior decoration and daily household use.

▶ **Generic Line** includes FMCG whose target consumer groups are the most price sensitive, or price-aware, customers. Products of the generic line assure the lowest price at Mercator. In April, a special advertising campaign was carried out.



▶ **Lumpi** includes food, cosmetics, and apparel for children aged up to 10 years, as well as toys, school stationery, and gift program. The products are currently in



a stage of active revision. All new products are under the supervision of the Institute of Public Health, Kranj, and the Ljubljana Pediatric Clinic.

- ▶ **Premium Line** is a newly conceived line intended for the customers with more exquisite taste. These high-quality products are made of the best ingredients, with less artificial additives; they are mostly of Slovenian origin.
- ▶ **The Wishing Table** includes products for the people who are short on time. It allows simple and fast preparation of a hearty meal. The offer includes individual products to be combined with others, products for immediate consumption, and refrigerated full meals that only require heating or cooking.
- ▶ **Healthy Living** includes products that contribute to the improvement of our customers' diets. The products meet at least one of the healthy food criteria: they are rich with fiber, have low fat content (particularly saturated fatty acids and cholesterol), low sugar and salt content, reduced caloric value.
- ▶ **The Kranj Cupcake** includes high-quality pastry products, emphasizing traditional hand-made delicacies. In 2009, we launched the redesign of the brand image and prepared a product catalogue.

Presence of individual private label lines and exclusive brands in foreign markets

	Mercator Line	Generic Line	Healthy Living	The Wishing Table	Lumpi	Grosuplje Bakery	Total Body Care	Ambient	Premium	Trebnik Mansion	TOTAL NR. OF LINES
Slovenia	x	x	x	x	x	x	x	x	x	x	10
Serbia	x	x	x	x	x		x	x			7
Croatia	x	x	x	x	x		x	x		x	8
Bosnia and Herzegovina	x	x	x	x	x		x	x			7
Montenegro	x	x			x			x			4
Bulgaria	x							x			2

In **Serbia**, we focused on the development of new Mercator Line and Generic Line products to improve our pricing competitiveness in 2009. Our goal is to improve the distinction and recognition of private label products and to increase their share in total revenues. Activities in 2009 included: presenting the private label products in regular monthly campaigns and in a special catalogue; rewarding our customers with packages of private label products upon openings and other events.

In **Bulgaria**, the Mercator Line is already present with both alimentary and non-alimentary products, and the Ambient Line currently includes the products of the non-alimentary segment. Customers were presented with the private label products in a special flyer.

In the course of 2009, the following long-term goals were pursued in **Bosnia and Herzegovina**: improving the distinctiveness and recognition, and increasing the number of private label products, and increasing the share of private label product sales in total sales revenues.

Sales promotion projects

Long-term Sales Promotion Projects

- ▶ The projects "**Every Day Low Price**" and "**National Basket**" were carried out throughout the region in 2009.
- ▶ **Members of the Slovenian Association of Free Trade Unions** are offered special benefits when paying with their ZSSS-DH card.
- ▶ We carried on the "**YES! Coupon**" campaign which includes rewarding shoppers who purchase at least EUR 50 worth of products on Tuesdays, with a coupon for 10 percent discount valid on the following Tuesday. The project is also in progress in Serbia, Montenegro, Croatia, and Bosnia and Herzegovina.
- ▶ In April 2009, we introduced the **Thursday discount for retirees / pensioners**. When spending at least EUR 20, customers in retirement will be rewarded with a 10 percent discount valid on the following Thursday. The project is being carried out in Slovenia and Bosnia and Herzegovina. In Montenegro, **Pensioner's Discount** campaign was carried out several times. Retirees were awarded with four coupons in a total value of EUR 70, and they were offered payment in four installments.
- ▶ We also carried out three customer loyalty programs: "Dormeo", "Tefal", and "Collect and Choose Zwilling!" This time, customer loyalty was rewarded with a 70-85 percent discount on the silverware of the renowned brand Zwilling.
- ▶ In Serbia, Croatia, and Bosnia and Herzegovina, project "**Dormeo**" was carried out in 2009. Customers who collected a certain number of sticker coupons were granted 60 percent discount on Dormeo products. In Croatia, similar campaign took place in the first half of the year with **Tognana** tea or coffee sets.
- ▶ In January and February 2009 the campaign "**Five per Day**" took place in Slovenia, allowing the customers to exchange discounts and coupons for fresh fruit.
- ▶ Special projects during the summer included a prize competition called "**With Mercator to the Football World Championship**."
- ▶ In Bosnia and Herzegovina, special projects included a prize competition "**Win a Mercedes**". In addition to the main prize, a Mercedes B car, several minor prizes were presented.
- ▶ In Croatia, we carried out prize competitions "**Free Shopping for 12 Months**" and "**Super School**". The "**Super Wednesday**" campaign was also carried out.

Short-term Sales Promotion Projects

Sales promotion communication was thoroughly revised. The main protagonists of the ads are our salespeople, who interact with the customers in a humorous way to present everyday situations at our stores.

- ▶ In 2009, the **Category Discount** activity was pursued further, offering at least 20 percent discount on a particular category from Friday to Monday. The campaign took place in Slovenia, Serbia, Croatia, Bulgaria, and Bosnia and Herzegovina.
- ▶ In April and May, activity "**Buy and Save!**" was carried out at hypermarkets. Each customer received a coupon for 5, 10, 25, 50, or 99 percent discount, effective for the current purchase. The campaign took place in Slovenia and Bosnia and Herzegovina.
- ▶ In May, we launched the campaign "**Special Weekend Offer**" which is carried out at the end of each month. The point of the campaign is to emphasize alimentary products appropriate for a particular time or season, and to price them favorably. The campaign was carried out in Slovenia, Bulgaria, Croatia, and Bosnia and Herzegovina.
- ▶ In December 2009 and January 2010, customers spending EUR 30 or more received a 25 percent discount coupon for the purchase of a daily ski pass at ski resorts Vogel, Krvavec, Cerklje, and Rogla. The campaign took place in Slovenia.
- ▶ In Serbia, campaign "**10 Percent Off on Sunday**" took place starting in May at all Roda megamarkets. In October, November, and December we also carried out the campaign at the hardware and electronics departments at Roda Cash&Carry stores and those Roda supermarkets that have such department.
- ▶ In December, we carried out the campaign "**New Year's Coupon**" which included rewarding customers spending more than 3,000 Serbian dinars with a 10 percent discount coupon valid in the next year. In the same period, we also carried out the prize competition "**1001 Tales of Winter Magic.**" The main prizes included 10 holidays for two in Venice, and three Hyundai automobiles.
- ▶ Immediately after our launch in Bulgaria, we started out "**Weekend at the Hypermarket**" campaign. In November, we also launched our **customer loyalty program** for "Magnifico glasses". Customers were presented with a pair of spectacles upon collecting a certain number of sticker coupons. At the end of the year, we launched the project "**New Year's Promotion**": children from daycare centers staged a puppet show and decorated 23 New Year's trees with toys of their selection. We also launched the "**Happy Hours**" project.
- ▶ In Bosnia and Herzegovina, we launched the "**Lock & Lock**" customer loyalty program in August, rewarding customers who spend more than 50 Convertible marks on Fridays. In December, we also carried out the "**Wednesday Coupon**" campaign, offering our customers discounts on selected products.

Other Activities

- ▶ **Hardware and electronics program:** In 2009, we carried out sales promotion campaigns to improve the distinctiveness of our hardware and electronics program among the consumers and to establish a reputation as a retailer offering technologically advanced and attractive, competitively priced products in Slovenia and abroad.
- ▶ **Clothing program and drugstores:** In order to promote the sales of certain seasonal products, several activities were conducted in Slovenia. We offered the service of fashion consulting in our major stores, and carried out regular campaigns and makeup days. In addition, activities of related purchases were also introduced. **In Serbia**, we offered "Happy Hours", "Buy 3, Pay for 2", and category discount campaigns. Mercator Pika card holders were sent a coupon for 20 percent discount on the following purchase. **In Bosnia**

and Herzegovina, regular campaigns were carried out at Beautique drugstores, in addition to special discounts on selected products, and discounts for Mercator Pika card holders. Sticker coupon collection campaign was also carried out. **In Croatia**, apparel and drugstore program included regular discount campaigns for particular groups of products, and our catalogues were advertised in magazines.

- ▶ **Intersport:** During the year, regular and additional campaigns took place in Slovenia in order to promote the sales of seasonal categories. We issued six program guides and four program catalogues. We carried out two international campaigns "Run Free Now" for the category of running, and sponsored selected events for amateur athletes. **In foreign markets**, we mostly focused on sales promotion projects: "Customers Win by 3:2", category discount, and related purchases. We developed and upgraded the presentation at the www.Intersport.si portal and set up a website at www.intersport.rs in Serbia.

STORE FORMATS

One characteristic feature of Mercator Group trade operations is the diversity of its retail network with various store formats both in the market program and in specialized stores of hardware and electronics, apparel and beauty, and sports program (Intersport).

As a response to the uncertain market conditions, changes in shopping habits of our customers, and changes in market trends, we started preparing a revision of Mercator hypermarket programs in Slovenia and abroad, which includes the following activities:

- ▶ redistributing the sales area among sales programs and categories;
- ▶ increasing sales area allocated for special offer goods (special offer aisles or islands within all programs, and final allocation of aisle compartments for targeted special offers);
- ▶ increasing the sales area intended for seasonal offer – establishing season-related aisles or islands where attractive season-related products can be promoted;
- ▶ more pronounced and effective labeling of special offers within regular and special offer sales areas.

Mercator Centers and Shopping Centers

Mercator centers are shopping centers with a wide offer of all Mercator programs, as well as offer of other attractive service providers operating in leased outlets, and the offer of complementary services. Hence, our customers are offered everything at one place. These facilities are located in major urban centers.

Roda centers are a format of modern shopping centers that combine the benefits of shopping at Roda megamarkets or supermarkets with the offer of many other attractive service providers, as well as some specialized Mercator programs.



Market Program Store Formats

Mercator hypermarkets are located in larger shopping centers where people not only do their major weekly shopping, but also socialize and spend their leisure time.



Mercator supermarkets and neighborhood stores are located in larger residential and commercial areas, and are intended for daily shopping.

Mercator comfort stores are located in central or, downtown areas of larger cities. Their program mix is adapted to the requirements of contemporary urban customers who are constantly in a rush. The emphasis is on fresh program and a wide assortment of ready-made food.



Mercator web store enables saving time and comfortable shopping without leaving your home.

Mercator Cash & Carry are conventional Cash & Carry stores selling only to companies, or only offering wholesale services. Assortment and sales area (larger, commercial packaging, larger quantities, units, and product packaging, functionality of store equipment, commissioning and delivery of the goods ordered, etc.) are adapted accordingly. These stores are located outside city centers, on the periphery of major cities; excellent traffic access is highly important for this store format.

At **discount stores**, customers are offered with rational shopping for basic FMCG, under the **Hura!** brand. The offer is based on the best ratio between price and quality, while providing the most competitive products in the market.

Roda megamarkets are larger stores offering affordably priced products, mostly to customers dosing their major weekly or monthly shopping. They are located in Roda centers where the offer of various supplementary service providers and complementary services allows socializing and enjoying leisure time.



Roda supermarkets and markets are located in major residential and commercial areas. They are intended primarily for daily shopping.

Roda Cash & Carry is an open-type Cash & Carry format serving for both legal persons and individuals (natural persons). Assortment and sales area are adapted accordingly. Open type Cash & Carry stores are located outside city centers, on the periphery of major cities; excellent traffic access and a large number of visitors are highly important for this store format.



Specialized Store Formats

Specialized store formats are developed for the purpose of providing activities that supplement our core activity or FMCG retail.

Hardware and electronics includes construction centers, independent combined hardware and electronics stores, and interior design and equipment stores.



Clothing program and drugstores comprises the following formats of textile stores, which differ by size, and the scope and level of offer: Fashion Avenue ('Avenija mode'), Modiana, and Outlet stores. The offer of beauty program is presented under the Beautique label (drugstores and perfumeries).



Mercator Group is the license holder for **Intersport**, the world's largest global chain of sports equipment stores. The license applies to the markets of Slovenia, Croatia, Bosnia and Herzegovina, Serbia, Montenegro, and Albania. Intersport stores are available to customers both within Mercator Centers as well as independently, i.e. as City Shops located in the centers of major cities. In tourist resorts, we are developing the so-called Ski & Resort stores.



Composition of Retail Units

Breakdown of the composition of Mercator Group retail units by types of stores, particular programs, and particular markets as at December 31st 2009

COUNTRY	SLOVENIA	SERBIA	CROATIA	BOSNIA AND HERZEGOVINA	MONTE-NEGRO	ALBANIA	BULGARIA	MERCATOR GROUP		
ACTIVITY	Number of units	Number of units	Number of units	Number of units	Number of units	Number of units	Number of units	Number of units	Gross sales area	Net sales area
Hypermarkets	20	12	14	6	1	1	1	55	264,048	174,834
Supermarkets	130	24	29	12	4	-	-	199	226,101	145,847
Superettes	279	25	42	2	4	-	-	352	149,325	84,176
Neighbour stores	67	3	15	2	1	-	-	88	14,146	7,611
Cash & Carry	12	2	-	-	-	-	-	14	35,055	22,991
Hard discount stores	16	-	-	-	-	-	-	16	13,134	9,209
TOTAL FMCG program	524	66	100	22	10	1	1	724	701,810	444,668
Technical program	96	7	14	-	-	-	-	117	158,283	90,794
Technical program	64	3	14	-	-	-	-	81	121,997	63,681
Furniture program	32	4	-	-	-	-	-	36	36,286	27,113
Clothing program and drugstores	97	19	30	13	-	-	-	159	69,142	57,877
Clothing program	80	10	30	9	-	-	-	129	65,601	55,004
Drugstores and perfumeries	17	9	-	4	-	-	-	30	3,541	2,873
Intersport	30	10	24	8	1	1	-	74	44,125	34,090
Restaurants	19	6	-	12	-	-	-	37	12,832	7,580
Other	11	-	-	-	-	-	-	11	197	189
TOTAL specialised programs	253	42	68	33	1	1	-	398	284,579	190,530
TOTAL	777	108	168	55	11	2	1	1,122	986,389	635,198
Franchise stores	225	-	76	-	-	-	-	301	53,928	34,938
TOTAL with franchise stores	1,002	108	244	55	11	2	1	1,423	1,040,317	670,136

Development of New Technologies and Services

In 2009, rollout of new technologies in our stores continued. In this year, self-service checkout cashiers were introduced in five Croatian hypermarkets and at hypermarket Škofja Loka. Tik Tak self-checkout cashiers are thus in operation in 29 Mercator hypermarkets and at two supermarkets. In Slovenia and Croatia combined, a total of 140 self-checkout cashiers are in operation, accounting for nearly 30 percent of all purchases.

Further Standardization of Store Formats

The standardization project in 2009 included 49 newly drafted standards, confirmed by the Store Format Standardization Project Council; the standards relate to the formats of hardware and electronics stores, Intersport stores, and market program store formats.

SUPPLIER RELATIONS AND LOGISTICS

Purchasing of Trade Goods and Supplier Relations

In 2009, looking for new, more favorable procurement sources and adjustment of offer to various segments of our customers remained the focus of our supplier relations efforts. Current market conditions have further increased the importance of a careful selection of appealing, marketable, affordably priced, yet high-quality products. We expanded the offer of our products in all private label lines, mostly by selecting the most favorable offers and quotations collected in public tenders; thus, purchasing prices were pushed down.

Particular attention was paid to the selection of products in short-term sales promotion projects. Responding to the said market conditions, we worked with our suppliers in order to provide high-quality offer of fast-moving consumer goods with added value at the end of the

year. In our permanent sales promotion projects such as "Every Day Low Price", particular care was devoted to the right selection of products, making sure that the top selling products of each category were made accessible to Mercator consumers at the most favorable price possible. We continued to decrease delivery failures, reduce inventories, and optimize our operations.

Upon our entry into the markets of Albania and Bulgaria, we negotiated with our suppliers to agree on attractive sales assortments; purchase agreements were signed with them.

Our supplier relations complied fully with the commitments accepted by the Competition Protection Office, Code on the Management of Trade Goods Supplier Relations, Working Instructions on Business Communication, and Working Instructions on Price Change Implementation, all of which were adopted as sound practice measures for providing compliance of company operations and its commercial transactions with the internal and external rules and regulations related to competition protection.

Logistics

In 2009, our logistics operations included efficient and successful provision of the agreed level of logistics services for the entities requiring them. Strategic programs for improvement of competitiveness were focused on further progress of the logistics infrastructure optimization project, with the following activities being at the forefront in the period:

In Slovenia:

- ▶ We have completed the first stage of implementing paperless operation and pursued the revision of fruit and vegetables distribution processes.
- ▶ In 2009, investment volume was decreased due to the economic crisis. As a result, activities related to the construction of the central logistics center in Želodnik were temporarily halted.

In foreign markets:

- ▶ In Croatia, a technological plan was prepared according to the agreement on the lease of a distribution center in Velika Nedelja.
- ▶ In Bosnia and Herzegovina, logistics facilities were relocated from the Rajlovac location to the Kakanj location, mostly for economic reasons.

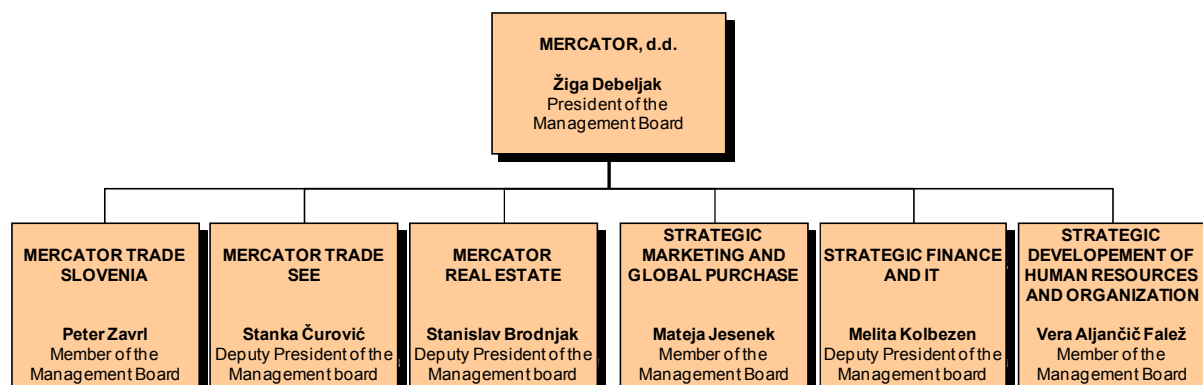
ORGANIZATION AND QUALITY OF OPERATIONS

In 2009, a number of organizational changes took place at the Mercator Group. We successfully passed independent assessments and audits for the international quality standards and earned new certificates. We carried out the activities of internal control and further pursued the activities of the strategic project of general optimization of Mercator Group operations.

Organizational Management

At its meeting held on September 28th 2009, the Management Board of Mercator, d.d., adopted the new macro-organizational structure effective as of January 1st 2010. The main reasons for reorganization are the necessity to improve local responsiveness in all markets, better adaptivity to consumer needs, improved efficiency of our operations, the need to

adapt the organizational complexity to international operations, and preparation for the option of monetization of our trade properties and facilities currently held in order to accelerate our development cycle.



Quality Standards

In 2009, two new certificates were awarded to Mercator, d.d.: ISO 14001 for environmental management system, and ISO 22000 for food safety management system; at Mercator - S, d.o.o., certificate ISO 9001 for quality management system and the HACCP certificate for food safety management were obtained.

All planned independent and internal assessments and audits of the ISO 9001 quality management system were carried out at the companies Mercator, d.d., Mercator - H, d.o.o., and Mercator - BH, d.o.o., as well as QWeb at v Mercator, d.d. Independent audit at Mercator, d.d., was carried out as integrated audit in 2009 and was the most extensive to date.

Customs Administration of the Republic of Slovenia, authorized in Slovenia for certification in compliance with the criteria for awarding the AEO status, awarded the "Status of Authorized Economic Operator" to the company Mercator, d.d. The AEO status indicates that Mercator is recognized as a safe and reliable partner in international trade in the entire European Community, particularly with regard to customs operations; as a result, it is eligible for additional benefits throughout the Community.

Electronic application for paperless management of incompliance, recommendations, and praises was introduced at Mercator, d.d. Further development of this application for optimizing and extending its use was also pursued. An application was developed to manage the electronic register of contracts and agreements, and the application for electronic management of councils was revised.

IT AND TELECOMMUNICATIONS

Consistently with the **strategic project of IT system revision**, the following activities were carried out in 2009:

- ▶ As a part of the project of **support function IT system revision**, we completed the extension of the use of the basic SAP modules in the companies Mercator - H, d.o.o.,

Mercator - BH, d.o.o., M - BL, d.o.o., and Mercator - B, e.o.o.d. The extension of the use of these modules was carried on by introducing the basic SAP modules at the company Mercator - S, d.o.o., in Serbia; as of January 1st 2010, these modules, too, are in use. For the company Mercator, d.d., we also set up a HCM SAP module (a system that enables capturing and processing information on organization, human resources, time, and compensation, at a single place) and the PY SAP module (a system enabling to run the entire process of employee compensation calculation and reporting on the payment of employee personal income to public institutions).

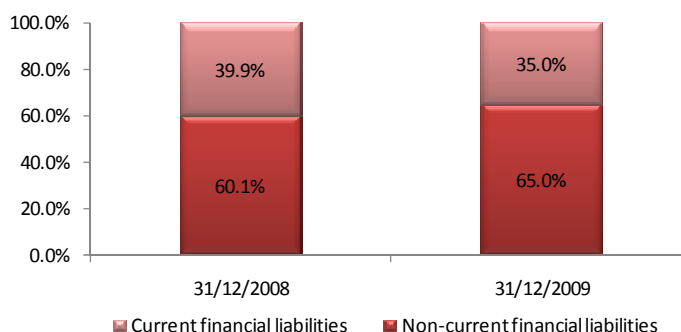
► As a part of the project of **material operation IT system revision**, or the implementation of the G.O.L.D. software solution for operation management in retail, logistics, and wholesales, we carried out the following:

- We have extended the use of G.O.L.D. CENTRAL module intended for editing and maintaining master data, managing procurement processes, and managing promotion activities;
- We connected 200 market format outlets in Slovenia to the G.O.L.D. SHOP module (background operations at the store) by integrating the new POS trade system.
- We provided support to material operation at the company Mercator - B, e.o.o.d.

FINANCIAL MANAGEMENT

Ratio between Current and Non-Current Financial Liabilities

Mercator managed to improve the maturity composition of the financial liabilities in favour of non-current financial liabilities.



Compared to 2008, the share of non-current financial liabilities rose by 4.9 percentage points.

Obtaining Sources of Financing and Liquidity Reserves Management

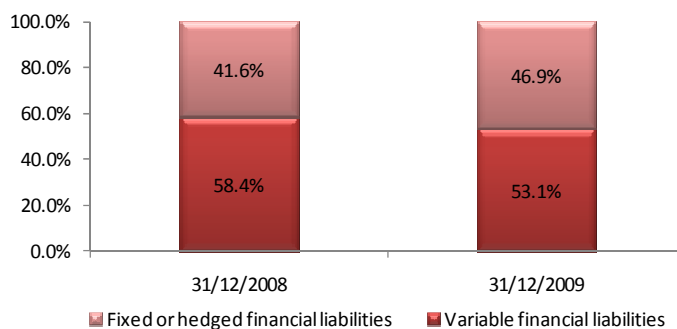
► In 2009, Mercator obtained short-term, as well as long-term bilateral loans and signed long-term financial lease agreements.

► In 2009, we saw a notable upward pressure on the interest rate margins, which is mostly the result of diminished liquidity of commercial banks, and shattered confidence in the interbank market.

► Particularly abroad, the use of long-term operating lease of trade facilities constructed for Mercator by local real-estate partners was resorted to as an increasingly important form of financing our investments.

- ▶ The average effective interest rate for bank loans of Mercator Group amounted to 4.09 percent in 2009.
- ▶ The Group pursued with its active management of liquidity reserves, i.e. of short term financial investments further in the year 2009 within the framework of its financial policy.

Ratio between variable and fixed or hedged financial liabilities of the Mercator Group



At Mercator, we are using derivative financial instruments to hedge the risk of rising interest rates.

MERCATOR SHARE AND OWNERSHIP STRUCTURE

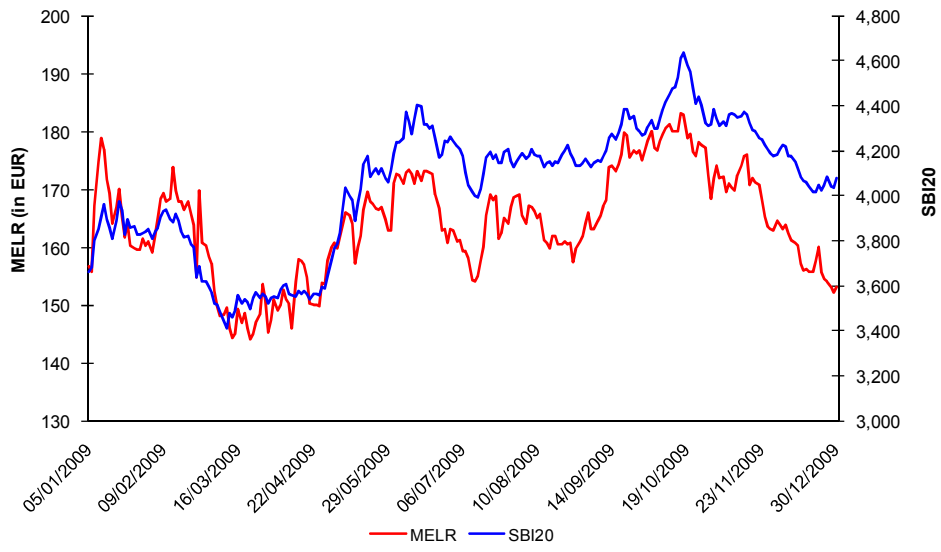
Mercator Share

As at December 31st 2009, the **share capital of the company Poslovni sistem Mercator, d.d.**, was divided into 3,765,361 shares. Nominal value per share amounts to EUR 41.73.

Shares of the company Poslovni sistem Mercator, d.d., are listed and traded in the **prime market of the Ljubljana Stock Exchange** (Ljubljanska borza, d.d.), under the trading code **MELR**.

At its meeting held on September 21st 2009, the Management Board of the company Poslovni sistem Mercator, d.d., adopted a resolution to launch preliminary preparation proceedings for the **issuance of up to 20 percent of new company share capital**, based on approved share capital, in order to secure in a timely manner additional financial funds to fuel any strategic combinations and alliances in the field of trade, real estate, or other activities.

Movement of average price per MELR share in 2009, compared to the movement of the SBI20 index



Key information for the shareholders

	December 31 st 2009	December 31 st 2008	Index 2009/2008
Number of shares registered in Court Register	3,765,361	3,765,361	100.0
Number of treasury shares	42,192	42,381	99.6
Market capitalization (in EUR)	576,740,344	595,228,267	96.9
Market value of share (in EUR)	153.17	158.08	96.9
Book value per share (in EUR)	211.13	209.79	100.6
Annual low (in EUR)	144.03	148.29	97.1
Annual high (in EUR)	183.11	343.58	53.3
Weighted average market price, excluding block and cross trades (in EUR)	164.83	243.37	67.7
Earnings per share (in EUR)	5.2	8.6	60.0
Price/earnings ratio (P/E)	29.6	18.3	161.5
Capital gains yield (in %)	-3.11	-52.81	-
Dividend yield (in %)	2.85	1.27	224.4
Total yield (in %)	-0.26	-51.54	-

Equity market capitalization is calculated as the product of the number of shares entered into Court Register as at December 31st, and the market price per share as at December 31st.

Basic net income per share is calculated as the ratio between net profit of the company Poslovni sistem Mercator, d.d., and the weighted average number of ordinary shares in the period at hand, excluding treasury shares.

Share book value is calculated as the ratio between the value of equity of the company Poslovni sistem Mercator, d.d., as at December 31st, and the weighted average number of ordinary shares in the period at hand, excluding treasury shares.

Price/Earning ratio is calculated as ratio between market price per share as at December 31st and net profit per share.

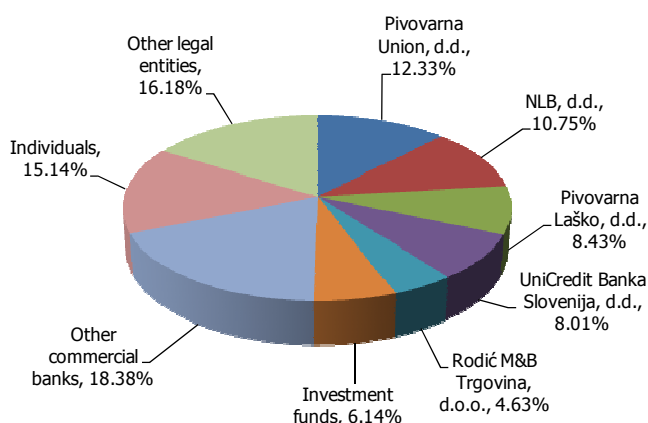
Capital gains yield is calculated as the ratio between market price per share as at December 31st of the period at hand, and the market price per share as at December 31th of previous year.

Dividend yield is calculated as the ratio between dividend paid per share and the market price per share as at December 31st.

Ownership Structure

As at December 31st 2009, the **Share Register** of the company Poslovni sistem Mercator, d.d., indicated **17,079 shareholders** or 225 less compared to the situation as at December 31st 2008.

As at December 31st 2009, the **ownership structure of the company Poslovni sistem Mercator, d.d.**, was as follows:



Major Shareholders

As at December 31st 2009, the following ten largest shareholders combined owned **60.51 percent** of the company:

Major shareholders	Country	Number of shares	Ownership share
1 Pivovarna Union, d.d.	Slovenia	464,390	12.33%
2 NLB, d.d.	Slovenia	404,832	10.75%
3 Pivovarna Laško, d.d.	Slovenia	317,498	8.43%
4 UniCredit Banka Slovenija, d.d.	Slovenia	301,437	8.01%
5 Rodić M&B Trgovina, d.o.o.	Serbia	174,517	4.63%
6 Banka Celje, d.d.	Slovenia	165,270	4.39%
7 Gorenjska banka, d.d.	Slovenia	142,920	3.80%
8 NFD 1 Delniški Investicijski Sklad, d.d.	Slovenia	107,211	2.85%
9 Abanka, d.d.	Slovenia	103,400	2.75%
10 Radenska, d.d.	Slovenia	96,952	2.57%
Total		2,278,427	60.51%

Foreign shareholders

As at December 31st 2009, the share of foreign investors in the company Poslovni sistem Mercator, d.d., amounted to **12.48 percent**, which is 0.24 percentage points more than at the end of 2008.

Shares held by Management Board members as at December 31st 2009

Name and surname	Number of shares	Ownership share
Žiga Debeljak	1,100	0.0292%
Vera Aljančič Falež	30	0.0008%
Mateja Jesenek	1,000	0.0266%
Peter Zavrl	60	0.0016%
Total	2,190	0.0582%

Shares held by Supervisory Board members as at December 31st 2009

Name and surname	Number of shares	Ownership share
President of Supervisory Board		
1. Robert Šega	0	0.0000%
Members of Supervisory Board (representatives of capital)		
2. Jadranka Dakič, deputy president	0	0.0000%
3. Štefan Vavti	0	0.0000%
4. Kristjan Verbič	0	0.0000%
Members of Supervisory Board (workers representatives)		
5. Mateja Širec	36	0.0010%
6. Jože Cvetek	2,000	0.0531%
7. Janez Strniša	0	0.0000%
8. Ivica Župetič	0	0.0000%
Total	2,036	0.0541%

Treasury shares

As at December 31st 2009, the company Poslovni sistem Mercator, d.d., held 42,192 treasury shares, which is 189 less than on December 31st 2008. In July 2009, the company Poslovni sistem Mercator, d.d., carried out a merger of the company Interier, d.o.o., with the company Poslovni sistem Mercator, d.d. In this transaction, 189 shares of the acquiring company were used as payment to minority shareholders, according to the exchange ratio defined in the merger agreement and audited by an independent auditor.

RISK MANAGEMENT

In 2009, Mercator Group operations were conducted against a backdrop of harsher and more strenuous economic conditions than initially planned: GDP growth was negative in all key markets. This was reflected in a notable decrease in demand in retail, in all markets of our operations; in addition, negative effects of the global financial crisis persisted. In such conditions, deliberate and prudent management of the risks encountered, while conducting operations in a changed economic environment, is all the more important for the Mercator Group.

Role, Principles, and Organization of the System

At Mercator, proactive risk management is the responsibility of the Mercator Group Risk Management Council; the Council is in charge of a systematic process of risk management.

Consistently with the need to monitor and analyze the risks from the aspects of several fields of expertise, The Risk Management Council includes the following three Committees for three key types of risk:

- ▶ **Business risks** related to company operation and its core activity;
- ▶ **Operational risks** related to executing and control of business processes and activities in the Mercator Group, and to the expenditures and costs incurred in the execution of business processes.
- ▶ **Financial risks** are those that may negatively affect the ability to generate cash flows, management of cash flows, maintaining the value of financial assets, and managing financial liabilities.

Risk management process

In 2008, the risk management process at Mercator Group was thoroughly revised. In 2009, the measures adopted to manage the key risks were assessed with a special internal audit.

To this end, the following was carried out:

- ▶ risks were reclassified and re-identified;
- ▶ sensitivity analysis was conducted to find how a particular risk, in case of occurrence, affects the gross cash flow from operating activities;
- ▶ marginal value for defining key risks was defined;
- ▶ risk management measures were defined.

Following are the benefits of systematic risk management:

- ▶ selection of more appropriate and successful strategies and more efficient tactics for attaining our goals;
- ▶ anticipation, timely identification of negative trends and events, and timely response;
- ▶ interaction between various fields and multi-faceted character of each set of problems is more successfully accounted for in business decisions and measures;
- ▶ improved performance;
- ▶ lesser negative volatility, or variance, of future business performance;
- ▶ lesser probability of business or financial problems;
- ▶ better relations with company stakeholders – customers, suppliers, banks, shareholders, employees;
- ▶ better information for adopting business decisions;
- ▶ better quality of planning future operations.

When implementing the revised risk management process, respective committees identified all risks to which Mercator Group is exposed or may be exposed, according to our estimate, in the following year or in the upcoming medium term period. In addition, the assessments of Mercator's exposure to particular types of risk were prepared. The assessments were made based on the level of probability of occurrence, and expected damage in case a particular loss events actually took place. Risks were defined by applying descriptive and quantitative criteria.

The objective behind the process revision is quantification of the Mercator Group's exposure to particular identified risk types, based on the sensitivity analysis, which shows the percentage of decrease in gross operating cash flow at the Mercator Group level, or at an individual company level, when a certain loss event, analyzed within the framework of a particular risk, actually occurs. Risks have been classified according to the level of effect on the gross operating cash flow and tolerable risk limits have been defined. In line with the defined policies, particular proposals for the management of certain types of risk have been prepared, which have already been implemented into the day-to-day decision-making processes and operations in certain fields. The measures taken form a basis for the planning of internal auditing processes in terms of annual audits of risk management measures adopted by the Risk Management Council.

Key Risks in 2009

At Mercator, we are constantly reexamining and analyzing the existing and potential new risks, as we devise and implement the measures for their management in daily operations. Particular attention is paid to the changes in economic conditions and their effect on individual areas of risk management. Following is a presentation of risks that were defined as key risks within their respective types, or groups of risks and were therefore most closely monitored in 2009.

Among the **business risks**, the following was defined as the key risk:

- ▶ Risk of a decline in the purchasing power:

As a result of harsh economic conditions, the risk of a decline in purchasing power remains high. Furthermore, changes in shopping habits and behavior of our customers have also been perceived, which affects the changes in both volume and composition of consumption. Bankruptcies and massive layoffs in some major systems considerably decreased the

purchasing power of some segments of the population. In all markets, we have adapted the marketing activities to the new conditions in order to provide a favorable offer for our customers, and to retain our revenue level.

The following were defined as key risks among the **financial risks**:

▶ Foreign currency risk:

For Mercator Group, foreign currency risk, defined as the possibility of a loss of economic benefit due to a change in the exchange rate of a particular currency, appears in the markets of Serbia and Croatia; therefore, we are actively monitoring the macroeconomic background of the changes in exchange rates and attempt to adapt our operations so as to mitigate the exposure to the foreign currency risk, by responding to general trends and by adapting our operations to reduce the exposure to this risk through natural hedging. Foreign exchange risk is among the key risks, and the Group is looking to hedge it with appropriate business measures as far as viable.

▶ Credit risk:

Due to the aggravation of the economic crisis, exposure of companies to liquidity problems is increasing. Hence, credit risk in Mercator's wholesale is also increasing, as is the possibility that receivables will only be collected, or settled, partly or not at all. Activities conducted in 2009 in order to mitigate the credit risk resulted in notable decrease of receivables to wholesale customers and other business partners, while only slightly decreasing sales to wholesale customers. The activities that were focused on in 2009 included the following:

- ▶ closer supervision of exposure to a single customer;
- ▶ proactive collection of receivables;
- ▶ insurance of receivables.

▶ Refinancing risks

This risk could become a key risk, if the conditions in the international financial markets were to be further aggravated.

Measures adopted to hedge the key risks at Mercator Group

At Mercator Group, the following measures were adopted to manage the key risks identified and described above.

▶ Measures adopted to manage the key risk of a decline in the purchasing power:

In order to manage the business processes and risks in a period of an economic slump and major oscillations in macroeconomic indicators, Mercator is carrying out measures in all fields in order to effectively manage its operations in these volatile conditions.

In terms of sales and purchasing, particular attention was paid to the markets of Slovenia and Croatia in 2009, as these are, in addition to Serbia, the key markets by revenues generated. Thus, we are working with the AT Kearney consulting company to establish a so-called pricing model. The model will take into account the macroeconomic changes in our environment (inflation, GDP, etc.), changes in the business environment (competitiveness, etc.), and other aspects in order to allow anticipating the effects on revenues generated by the retail network in Slovenia at several levels (product, category, entire network).

Introduction of business result modeling based on macro- and micro-economic criteria also enables greater reliability of forecasting the effects of changes in the macro and micro environment. Furthermore, it allows better flexibility of the company and adaptability of its retail pricing, which in turn results in better adaptability to the conditions in the environment, including a potential decline in consumer purchasing power. Last but not least, it allows control over the financial investment of cutting prices and profit margins – an investment that may be a required response to such event.

In marketing, operating activities are conducted with maximum commitment. High level of promotional activities and constant presence in the marketing mix allows us to provide the conditions for maintaining sales at the high levels from previous years. At the level of strategic marketing, we are making extra efforts in setting up the Customer Relationship Management system; using transaction databases, it will allow us a more accurate insight into the desires and needs of our customers. Simultaneously, support to commercial and marketing activities also includes setting up continuous monitoring of key consumer behavior indicators related to shopping for fast-moving consumer goods, in a form that will allow instant calculation of correlation between the said parameters.

▶ Measures adopted to manage foreign currency risk:

For Mercator, foreign currency risk is present in the markets of Serbia and Croatia. In other markets, legal tender is either euro or a currency pegged to it. In 2009, foreign currency risk was identified as a key risk; as a result, the following measures were adopted to manage it:

- ▶ constant monitoring of macroeconomic background of the changes in the exchange rate at hand, and other related macroeconomic indicators and trends;
- ▶ based on the general trends and expectations, we are looking to adapt our operations, as far as possible, in such way that it is naturally unexposed to foreign currency risk;
- ▶ in case of increased risk, we decided, given the estimated level of our exposure, to enter forward or option contracts by which the parent company Poslovni sistem Mercator, d.d., protects its subsidiaries from the foreign currency risk.

Foreign currency risk is particularly notable because our subsidiaries in Serbia and Croatia have financial liabilities denominated in euros. In order to financially evaluate the foreign currency risks, sensitivity analysis was carried out, measuring Mercator Group sensitivity to the changes in exchange rates.

▶ Measures adopted to manage credit risk:

Due to the aggravation of the economic crisis, exposure of companies to liquidity issues is increasing. Simultaneously, credit risk of Mercator's wholesale is increasing. At Mercator, we responded to the changes in our environment by defining the measures to reduce the exposure to wholesale credit risk. In risk analysis for 2009, wholesale credit risk was defined as a key risk; therefore, the following risk management measures were adopted:

- ▶ Securing first-class credit insurance from customers with lower credit rating;
- ▶ Continuous monitoring of customers defaulting on their payments and restricting exposure to individual customers;
- ▶ reducing the number of days of default on payments after which further payments are blocked;
- ▶ proactive procedures of receivables collection - improved coordination between commercial and financial function;
- ▶ more active legal proceedings;
- ▶ promoting mutual and chain offsetting with customers, where possible.

Credit risk related to receivables from purchases with Mercator Pika card involves a significant probability that claims resulting from deferred payment, or customer crediting, will be settled only partly or not at all. Risk analysis for 2009 defined credit risk related to Mercator Pika card as a key risk.

The following measures were adopted to manage it:

- ▶ proactive collection of receivables from Mercator Pika card holders;
- ▶ introducing a new credit scoring model defining the opening limits to customers paying with the Mercator Pika card.

▶ Measures adopted to manage the key risk of refinancing:

In order to limit the refinancing risk, we agreed with all commercial banks already in the beginning of the year on refinancing the loans due for payment in 2009. We reached an agreement to convert a part of our short-term loans into long-term bilateral loans or long-term financial leases, thus reducing the refinancing risk. In the course of 2009, we also managed to improve the maturity composition of financing sources. Since 2008, we are actively managing our liquidity reserves, thus hedging the liquidity and refinancing risks.

Estimation of the risk exposure of Mercator Group

The Management Board estimates that total exposure of Mercator Group to business, financing, and operational risks, as at December 31st 2009, considering the current assumption for further development of the aspects of economic environment in 2010, is at a **moderate level**.

It should furthermore be noted that there is a considerable uncertainty with regard to the following:

- ▶ conditions in financial markets;
- ▶ further effects of a sluggish economic recovery; and
- ▶ future macroeconomic situation in the countries of the Western Balkans.

Should any major changes occur, relative to the current expectations, with regard to the key aspects of our business and economic environment, as listed above, the exposure of Mercator Group to:

- ▶ risk of attaining the planned amount of revenues from sales, resulting from a decline in purchasing power;
- ▶ risk of refinancing of short-term financial liabilities;
- ▶ foreign currency risk, particularly in Serbia and Croatia;
- ▶ and/or any other risks.

could become considerable, or high, despite the measures introduced to hedge them.

Therefore, the company will update each quarter its assessment of exposure to risks, according to the development of the aspects of business and economic environment; these reassessments will be reported on in interim, or quarterly, business reports.

CORPORATE SOCIAL RESPONSIBILITY

Socially accountable action has long surpassed the mere system of communication management of the values of the company and its stakeholders, to become a real value of the company, which is managed and developed through a wide array of corporate governance.

Sponsorship, donations, and participation in humanitarian campaigns are an important part of the strategy of comprehensive socially responsible conduct of the Mercator Group.

In Slovenia, our traditional central humanitarian campaign was dedicated to those who are unexpectedly facing social distress due to the effects of the global economic crisis. The campaign called "Kind Deeds Stem from Kind Words" collected one hundred thousand kind words as anyone was given the opportunity to symbolically support our campaign by selecting a kind word from Mercator webpage or special screens installed at Mercator shopping centers. The words most often selected were "kindness, safety, and love". We worked with our partners and suppliers to turn kind words into actions and provided actual aid for over one hundred thousand people. We donated half a million euros worth of food, school accessories for children, hygiene or body care products, and other essentials to Red Cross and Caritas Slovenia.

In addition, we supported numerous humanitarian, sports, culture, scientific, educational, and other projects and organizations engaging in socially responsible efforts in all markets of our operations.



CARE FOR THE ENVIRONMENT

Mercator operations are conducted while bearing in mind the generations to come. We are aware that as Slovenia's largest company, which is furthermore increasingly becoming an international corporation, we are in a position to contribute substantially to the protection and preservation of the environment, even though our activities are not among those most harmful to it. As a **socially responsible enterprise aware of the importance of relieving the burden brought upon the environment**, we are continuously improving our business processes to make them more environmentally friendly.

Environmental policy and our business partners

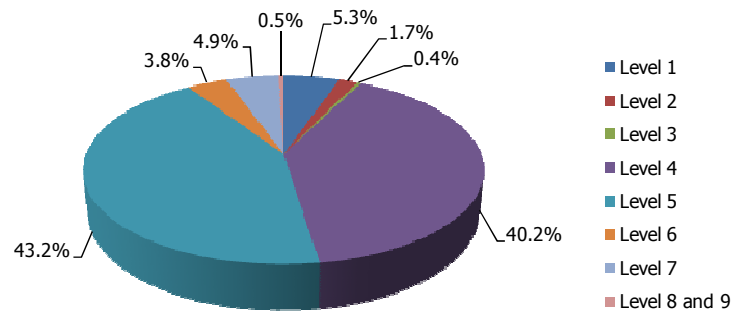
Mercator Group has precisely defined its environmental policy which is being consistently pursued as one of the key principles of our operations. Thus, we have already made a commitment to continuously improve our environmental management, prevent pollution, as well to comply with all legislative provision relevant to the Group. Our environmental policy also represents a framework for cooperation with our business partners on the issues concerning environmental management.

EMPLOYEE DEVELOPMENT

Number of employees

As at December 31st 2009, Mercator Group had 21,404 employees, of which 40.1 percent were employed abroad. The controlling company Poslovni sistem Mercator, d.d., employs 12,297 workers which is 57.5 percent of the Group's total.

Breakdown by level of education



Most Mercator employees have completed fifth-degree education. Composition by education is improving, however, as progress is notable particularly with employees holding 6th, 7th and 8th degree education.

Employee Relations

► Talent development and career planning

In 2009, the year of crisis, talent development and career planning was adapted to the prevailing conditions.

► We organized a **key employee council** to celebrate Mercator's **60th anniversary**. The council, attended by over 1,700 key employees, also hosted the President of the Republic of Slovenia, Dr. Danilo Türk.



► In Croatia and Serbia, **store manager training** was carried out. In Slovenia, we provided a somewhat abridged program of **deputy store manager training** in which one third of deputies for market program were included.

► In Slovenia, we organized **business workshops for directors and heads of services or departments**. This time, workshops took place at our head offices in Ljubljana in order to save on travel expenses and lease of venues.

► **Mercator International Business Academy** hosted the third group of 29 promising employees. Highly talented employees from nontrade subsidiaries were included in the Academy for the first time.



- ▶ The scope of training, number of attendants and costs of training declined slightly in 2009; however, **all essential training requirements** in the Mercator Group were successfully met both with regard to formal education and training and with regard to mandatory and functional training and training for personal development.
- ▶ 316 executive, managerial, and expert employees, which are in every day relations with suppliers, attended the seminar "**Presentation of Commitments to the Competition Protection Office**".
- ▶ 1,107 employees from administrative services completed the training on **occupational health and safety** and **fire safety**, in the form of self-training which included pre-programd materials and a relevant test.
- ▶ We have carried on the selection process and training of new coaches for our **coaching and mentorship network** in retail. A total of 580 fully trained coaches are currently active in Mercator Group; in 2009, they trained a total of 9,771 sales employees. The coaches regularly update their training in cooperation with our suppliers.
- ▶ In Slovenia, we organized **training** for 144 employees from Bulgaria, Albania, Bosnia and Herzegovina, and Montenegro.
- ▶ 743 high school and university students were admitted for **practical training**.
- ▶ We also encourage formal education of our employees: 278 were enabled to attend **part time studies**.
- ▶ We organized the **9th meeting of in-house instructors** at Mercator, d.d. The meeting was attended by nearly 400 in-house instructors. 27 employees received awards for special achievements and for their work as mentors, lecturers, instructors, or coaches.

▶ **Staffing and recruitment**

- ▶ Economic crisis profoundly affected staffing and recruitment at the company. Since hiring was scaled down and often completely halted, the number of employment applications soared. At the company Poslovni sistem Mercator, d.d., 8,413 job applications were received, and 823 applicants were newly employed, most of them in retail. In 2009, staffing was also focused on foreign markets: 814 people were hired in Bosnia and Herzegovina, Bulgaria, Albania, and Montenegro, combined.

- ▶ We have set up our **employment portal** at www.mercator.si/kariera, and revised the HRM website in English. Thus, we cut costs of HRM advertising.



- ▶ We also adopted the **HRM standard** for the company Poslovni sistem Mercator, d.d.

▶ **Motivation and compensation**

- ▶ Responding to the harsh economic conditions and a decline in the standard of living, the company Poslovni sistem Mercator, d.d., decided to implement a **solidarity redistribution of salaries** and performance bonuses from those with higher total rewards to those with lower ones. Hence, gross compensation of the Management Board President was cut by 25

percent, salary of Management Board members were cut by 15 percent, and salaries of other employees with individual employment contracts were reduced by 10 percent. Other employees in the highest salary categories saw their performance bonus cut by 3-5 percent, while the employees in the lower salary categories saw an increase in this bonus by 3-7 percent.

▶ Representatives of relevant trade unions were invited to take part in the **expert task force on total reward system**, whose purpose is constant monitoring and improvement of the total reward system at the parent company.

▶ An award ceremony was held in June. Twenty most distinguished employees were presented with the traditional "**Mercator Award**" for 2008.



▶ We completed our **motivation trips to Vogel** which were attended by 17 international teams of managers, or a total of 298 employees.

▶ We organized the third competition for **The Best Boss**, selecting 16 "best bosses" at the parent company for the year 2009.

▶ 2009 was a successful year for our HRM officers, as they received the following awards:

- **Human Resource Manager of the Year 2009**, awarded by the company Planet GV, was presented to Management Board member, Vera Aljančič Falež.
- Slovenian Institute for Adult Education presented an **Award for distinguished expert achievements** in the field of employee training and education at Mercator.
- Mercator project "Humanitarian Aspect of HRM Function at Mercator" received the **award for innovative human resource practice**, presented by the company Forum Media.
- HRM project **Promoting Health at Mercator** won the 2nd prize HRM projects in 2009; the prize is awarded by the company Planet GV.

▶ **Dialogue with the employees**

▶ From March 20th to June 26th 2009, **annual meetings** of leaders with all employees took place in all markets.

▶ In Slovenia, five regular and one special editions of our **internal magazine** were published. In Serbia and Croatia, five regular and two special editions were issued, and in Bosnia and Herzegovina and Montenegro, three editions were published.



▶ We have continued our regular monthly **meetings with representatives of relevant trade unions** and organized **meetings with the Management Board** upon discussions on quarterly business reports.

▶ Retail and human resource management visited several hypermarkets in Slovenia in the course of fall 2009, to **talk to the employees** on their work, possibilities of improvement, and work conditions.

SELECTED FINANCIAL DATA FOR 2009

All following presented financial data stem from the audited annual report of Mercator Group and the Company Poslovni Sistem Mercator d.d. for the year 2009.

Net sales revenues

Net sales revenues reached EUR 2,643 million which, assuming constant exchange rates, is 0.6 percent more than in 2008. However, that translates into a fall of 2.4 percent of net sales revenues when taken into account the changes in exchange rates.

Gross cash flow from operating activities before rental expenses

Gross cash flow from operating activities before rental expenses (EBITDAR) amounted to EUR 196,619 thousand, which is only 0.8 percent less than in 2008, assuming constant exchange rates. However, when taking into account the changes in exchange rates, gross cash flow from operating activities before rental expenses was lower by 3.8 percent in comparison to the previous year.

Gross cash flow from operating activities (EBITDA), amounted to EUR 167,296 thousand in 2009, which, assuming constant exchange rates, is 3.0 percent less than the year before. When considering changes in exchange rates, gross cash flow from operating activities was lower by 5.4 percent compared to the previous year.

Results

In 2009, Mercator Group's results from operating activities (operating profit) amounted to EUR 71,842 thousand, which is 28.4 percent less than in 2008. In 2008, the operating profit was notably affected by net proceeds from disposal of fixed assets (property, plant, and equipment), and other net revenues generated by extraordinary or non-recurring events (elimination of provisions). Excluding the extraordinary effects in both years, the comparable results from operating activities (operating profit) would have amounted to EUR 73,502 thousand, or 18.5 percent less than in 2008 (EUR 90,180 thousand).

Mercator Group's profit before income tax in 2009 amounted to EUR 25,196 thousand, which is 49.6 percent less than in 2008. In addition to the extraordinary effects described above, profit before income tax was also affected by net proceeds from disposal of financial assets, which were quite considerable in 2008 and almost negligible in 2009. Eliminating the extraordinary effects in both years, the comparable profit before income tax in 2009, amounting to EUR 27,056 thousand, is 20.5 percent lower than in 2008 (EUR 34,044 thousand).

Mercator Group realized a net profit of EUR 21.1 million, which is 48.2 percent less than in year 2008, due to the strained economic conditions and lower volume of generated extraordinary income compared to 2008.

Equity

As at December 31st the share capital of company Poslovni sistem Mercator, d.d., amounted to EUR 786,088 thousand and compared to 2008 it has increased by 0.6 percent. Book value per share as at December 31st 2009 amounted to EUR 211.13.