Mercator

Annual report 2012

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INTRODUCTION

REPORT BY THE PRESIDENT OF THE MANAGEMENT BOARD

A change in strategy and focus on the core activity

Stopping the negative trends in Mercator's performance was the top priority for the new Management Board and all employees in 2012. Declining market share, poorer cost efficiency and underperforming investments from the past, combined with the escalating effects of the economic crisis, negative currency translation differences, and dwindling purchasing power, drove the operating results into the red. Our approach to this challenge was realistic, but also optimistic. After taking office, the Management Board developed a new strategy based on four key pillars: optimization, focus, profitability, and growth.

Mercator is currently in the restructuring stage which is necessary because of a lack of focus in the strategy in the past. In our core activity, our performance is sound and positive; we saw good results in our key markets. Although the result for 2012 is negative, Mercator Group is financially solid. It has firm foundations and above all the potential to successfully pursue its vision of becoming the most successful and the most efficient retailer in the region. We wish to do whatever it takes for a satisfied customer to recognize us as the best retailer that offers everything a discount store can offer, and much more.

Countering the negative trends

In order to be truly efficient in attaining the short-term goals laid down, we immediately launched especially the measures to cut costs, deleverage, and reorganize our business logistics processes. We soon saw the initial palpable results as we reduced our debt by over EUR 90 million and net working capital for EUR 135 million, introduced a more austere investment policy, improved the cost efficiency in all areas of our business operations, and stopped the trends of declining market shares. These were only the first steps in the process of reviving Mercator. In the long run, we are looking to boost productivity by three percent per year until 2016 and to maximize the returns for our shareholders.

We commenced the restructuring of our retail network in order to adjust it to new operating conditions.

Growth expectations in markets that Mercator entered relatively late are feeble. Thus, we have adopted a strategic decision to withdraw from Albania and Bulgaria, and to concentrate on the five key markets in terms of geographical focus, and on the fast-moving consumer goods program in terms of business segment focus. FMCG, which is our core activity, accounts for 92 percent of our sales and it has the best potential for future operations. We started to reap the synergies in the markets of Slovenia and Croatia where the retail area and offer are being adjusted to the local microenvironment. We will restructure and revive our subsidiaries Modiana and Mercator Tehnika where we already implemented a new strategy based on optimization of sales network and stronger focus on economically sustainable, i.e. profitable programs.

It is especially important that the positive effects of immediate measures have been seen in the market. In Slovenia, we succeeded in stopping the trend of declining market shares, which is a great success. Similar measures are being implemented in Croatia and Bosnia and Herzegovina; in Serbia we are the only major retailer seeing considerable increase in market share; in Montenegro we are the market leaders.

Offer our customers what they need – every step of the way

In retail, bigger is better. At the moment, Mercator is proudly managing over 1.5 million of square meters of retail area. However, customers increasingly prefer smaller neighbourhood stores. Therefore, activities for growth must, as a rule, be carried out in smaller store formats and in the markets where such growth is attainable – where

Mercator is synonymous with high quality, service, and wide choice.

Mercator enjoys the advantage of having an extensive store network, especially regarding smaller neighbourhood stores where people shop daily. However, consumer confidence in Slovenia plummeted in 2012. Effect of the crisis as perceived by individuals in their everyday life was stronger in 2012 than in the year before. It is therefore our mission to convince our customers at the stores or at the point of sale that we know their needs and desires, and that our offer and services come closest to them. Our refurbishment activities were particularly focused on smaller stores, making sure the shopping experience was smoother and streamlined. Above all, we are looking to offer more fresh, local, new products; to communicate even more directly; and to change the perception of our pricing. We started developing new projects for our customers. In Slovenia, these include farmer's markets offering fruit and vegetables, new varieties of bread with traditional regional characteristics, and revival of our culinary heritage. In each market of our operations, we started making use of our own advantages and stressing the local characteristics that represent added value for our customers, such as the "local basket" and products of our private label lines. We are transferring good practices among all Mercator companies.

Our desire to come even closer to our customers was also manifest in our corporate campaign Steps. We gave our customers the opportunity to take part in the creation of our advertisements and to contribute their video clips and photos of their memorable experience. This, too, was in fact an innovative communication approach and another step towards changes and fresh ideas that can bring about a breakthrough and change.

We are facing challenges both past and present; yet we are convinced we have the right answers. We shall do whatever it takes for a satisfied customer to recognize us as the best retailer offering everything a discount store can offer, and much more.

Restoring confidence and smiles

I am honestly pleased by the professional attitude of the employees, their loyalty, and readiness for change. This is a great added value for the company as there is a lot of work to be done. The trends and achievements of 2012 show we are on the right track. We wish to boost the confidence of all stakeholders by delivering returns for the shareholders, consolidating our partner network of suppliers in all markets, convincing the customers that we are the best choice, and bringing the smiles back to the faces of our employees. We are facing challenges both past and present; yet we are convinced we have the right answers. These arduous conditions open up opportunities for changes and new solutions that will grant Mercator the place it deserves – not merely the best neighbour, but also the best retailer in the region. I thank everyone who has confidence in us and who supports us in our efforts.

Toni Balažič
President of the Management Board

Ljubljana, February 27, 2013

SUPERVISORY BOARD REPORT

Supervisory Board Activities

Pursuant to the legislation and company Articles of Association, operations of the company Poslovni sistem Mercator, d.d., as the controlling company of the Mercator Group was supervised in 2012 by a Supervisory Board which met at thirteen regular sessions in the course of the year.

At the session held on April 10, 2012 the changes in Supervisory Board were confirmed. Thus, the Supervisory Board includes the following members: Matej Lahovnik, PhD, (Supervisory Board chairman), Rok Rozman (deputy chairman), Boris Galić, Zdenko Podlesnik, and Marjeta Zevnik – all representing the shareholders, and Mateja Širec, Ivan Valand, and Sandi Leban – representing the employees.

At the meetings, the Supervisory Board mostly discussed current performance and property of the company Mercator, d.d., and the Mercator Group, interim reports and Annual Report; it supervised the Management Board activities, investment activities, implementation of major projects, financial policy and financial position, annual business plans, and implementation of the resolutions adopted by the Supervisory Board.

Major Supervisory Board resolutions

In 2012, the Supervisory Board discussed and adopted the audited financial statements for 2011 for the company Poslovni sistem Mercator, d.d., and the Mercator Group, and took note of the quarterly performance and results of the company Poslovni sistem Mercator, d.d., and the Mercator Group in 2012.

In addition, the Supervisory Board discussed other current issues and adopted the following major resolutions:

- discussed and adopted the Annual Report for the company Poslovni sistem Mercator, d.d., and the Mercator Group for the year 2011, and confirmed the wording of the Supervisory Board Report on the Annual Report audit, and the opinion to the proposal on the allocation of distributable profit for 2011;
- appointed four members of the Audit Committee, of which two were independent members;
- appointed the Human Resource Committee of the Mercator, d.d., Supervisory Board;
- confirmed the proposal for Shareholders Assembly provided by the Audit Committee to appoint the company KPMG Slovenija, d.o.o., to audit the financial statements of the company Poslovni sistem Mercator, d.d., and the Mercator Group for the year 2012;
- adopted the Business Reports of the Mercator Group and the company Mercator, d.d., for the periods I-III 2012, I-VI 2012, and I-IX 2012;
- adopted the report on the merger of the company VESNA, trade company, d.d., to Mercator, d.d.;
- on the basis of submitted statement of resignation the Supervisory Board and the Management Board agreed on recalled of the President of the Management Board and other Management Board members, relieving them of their duties; and appointed a new President of the Management Board and Management Board members for a term of five years;
- adopted the Management Board Act of Poslovni sistem Mercator, d.d., which specifies the number of Management Board members and their respective duties and powers;
- took note of the activities in real estate monetization,
- confirmed the Mercator Group Strategy and the Medium-term business plan for the period 2013-2016;
- confirmed the launch of activities to divest the company Mercator – Emba, d.d.; activities to merge the subsidiaries Intersport, Modiana, Tehnika, and M - Optima to Mercator companies in individual markets; and start of incorporation of a holding company in Montenegro;
- discussed the report on the findings of the Benchmark analysis (comparative study of competition) in the alimentary and FMCG trade industry for 2011,

- confirmed the Business Plan for the year 2013.

Activities of the Audit Committee

The Audit Committee consisting of chairwoman Jadranka Dakič (Supervisory Board member) and two members Jože Cvetek (Supervisory Board member) and Peter Ribarič, MSc, (independent expert on accounting and auditing) held two meetings in 2012: on February 15, 2012 and March 3, 2012. At these meetings, the Audit

Committee adopted the following notable resolutions:

- The Audit Committee discussed and commented the Annual Report of the company Mercator, d.d., and the Mercator Group for the year 2011.
- The Audit Committee was presented the report by the independent certified auditor on the progress and findings of the second stage of the audit carried out at the company Poslovni sistem Mercator, d.d., and the Mercator Group in 2011, and discussed this report with the independent auditor.
- The Audit Committee discussed and confirmed the offer for the audit of the company Mercator, d.d., and Mercator Group for the year 2012, and proposed to the Supervisory Board to select the auditing company KPMG Slovenia, d.o.o., as the company auditor; however, that the key auditing partner be changed pursuant to the Corporate Governance Code.

On April 10, a new four-member Audit Committee was appointed, consisting of chairwoman Marjeta Zevnik (Supervisory Board member), and three members: Rok Rozman, MSc, (Supervisory Board member), and Sergeja Slapničar, PhD, and Aleksander Igličar, MSc, (both independent experts on accounting and auditing). The Committee held five meetings in 2012. The sessions took place on May 14, June 11, August 20, November 12, and December 10, 2012. The Audit Committee adopted the following major resolutions:

- the Audit Committee confirmed the revised Rules of Procedure of the Audit Committee of the Supervisory Board of the company Poslovni sistem Mercator, d.d.;
- the Audit Committee discussed the auditor's letter to the company Management Board (the management letter) for the year 2011;
- the Audit Committee examined, commented on, and provided suggestions and recommendations to the Risk Management Report of the company Mercator, d.d., and the Mercator Group for the year 2011;
- the Audit Committee examined and proposed suggestions for improvement of the Business Reports of the company Mercator, d.d., and the Mercator Group for the periods I-III 2012, I-VI 2012, and I-IX 2012;
- the Audit Committee was presented the report on transfer pricing and corporate income tax accounting for the company Mercator, d.d., for 2011;
- the Audit Committee was presented the real estate monetization project of the company Mercator, d.d.;
- the Audit Committee discussed the report on the findings of the Benchmark analysis (comparative study of competition) in the alimentary and FMCG trade industry for 2011;
- the Audit Committee was informed about the activities of the Horizontal Monitoring project;
- the Audit Committee ordered an independent evaluation of internal audit and on the basis of conclusions of external appraisers ordered a change in the organizational placement of internal audit in order to increase its role in the company;
- the Audit Committee confirmed the plan of internal audits for 2012;
- the Audit Committee was presented the work of internal audit in 2012, and provided recommendations for improvements;
- the Audit Committee was presented the report of the independent evaluation of the work of internal audit at Mercator, d.d.;
- the Audit Committee examined the work of internal control in 2011;
- the Audit Committee gave an offer to hire a new external appraiser for valuation of real estate;
- the Audit Committee examined the offer for appraisal of real estate held by Mercator Group companies;
- the Audit Committee was presented the report by the independent certified auditor

on the progress and findings of the first stage of the audit carried out at the company Poslovni sistem Mercator, d.d., and the Mercator Group in 2012;

- the Audit Committee was presented the internal audit plan for the year 2013; the Committee also provided recommendations for the plan's improvement;
- the Audit Committee was presented the reports on extraordinary independent audits;
- The Audit Committee adopted its draft session schedule for the year 2013.

Semiannual and Annual Report for 2012

The Supervisory Board examined the non-audited Semi-annual Business Report of the company and the Mercator Group for the period I-VI 2012 at their session held on August 22, 2012. The company announced its non-audited semiannual report pursuant to the relevant legislation and the Rules and Regulations of the Ljubljana Stock Exchange, d.d.

At its regular meeting held on March 3, 2013 the Supervisory Board discussed the audited non-consolidated and audited consolidated Annual Report for the year 2012, audited by the auditing company KPMG Slovenija, podjetje za revidiranje, d.o.o., Ljubljana. The Annual Report had previously been discussed on March 4, 2013 by the Audit Committee of Mercator, d.d. Also present at this Audit Committee session was the certified auditor who provided any additional explanations required. On February 18, 2013, the auditing company issued an unqualified opinion on the non-consolidated and consolidated Annual Report. Supervisory Board did not have any objections to the certified auditor's reports and concurred with both.
The Supervisory Board had no objections to the submitted Annual Report of the company Poslovni sistem Mercator, d.d., and the Mercator Group for 2012, and confirmed it unanimously at the meeting held on March 6, 2013.

In 2012, the company Poslovni sistem Mercator, d.d., ran a net loss of EUR 77,602,465.26. The loss was covered from the following components of equity:

- retained earnings in the amount of EUR 10,337,126.70; and
- other revenue reserves in the amount of EUR 67,265,338.56.

As at December 31, 2012, the company did not report distributable loss or distributable profit.

This Report was issued by the Supervisory Board pursuant to the provisions of Article 282 of the Companies Act. The Report is intended for the Shareholders Assembly.

Matej Lahovnik
Supervisory Board Chairman

Ljubljana, March 6, 2013

OVERVIEW OF YEAR 2012 BY MARKETS

MERCATOR GROUP
Revenue: 2,873 mn EUR
Number of employees: 23,920
Number of retail units: 1,600
Gross sales area: 1,220,869 m²

SLOVENIA
31-33% market share of FMCG
Revenue: 1,618 mn EUR
Number of employees: 11,794
Number of retail units: 952
Gross sales area: 602,465 m²

CROATIA
4-5 % market share of FMCG
Revenue: 381 mn EUR
Number of employees: 3,627
Number of retail units: 244
Gross sales area: 250,622 m²

SERBIA
8-9 % market share of FMCG
Revenue: 561 mn EUR
Number of employees: 4,764
Number of retail units: 199
Gross sales area: 233,956 m²

BOSNIA AND HERZEGOVINA
6-7 % market share of FMCG
Revenue: 194 mn EUR
Number of employees: 2,004
Number of retail units: 113
Gross sales area: 77,821 m²

MONTENEGRO
18-19 % market share of FMCG
Revenue: 105 mn EUR
Number of employees: 1,417
Number of retail units: 85
Gross sales area: 38,384 m²

BULGARIA
< 0,5 % market share of FMCG
Revenue: 9 mn EUR
Number of employees: 205
Number of retail units: 4
Gross sales area: 11,645 m²

ALBANIA
1% market share of FMCG
Revenue: 4 mn EUR
Number of employees: 109
Number of retail units: 3
Gross sales area: 5,975 m²

PERFORMANCE HIGHLIGHTS

Summary of Mercator Group operations in the period 2007-2012

	2007	2008	2009	2010	2011 restated	2012	Index 2012/2011 restated
INCOME STATEMENT							
Revenue (in EUR 000)	2,445,258	2,708,560	2,643,315	2,781,604	2,870,971	2,873,186	100.1
Results from operating activities (in EUR 000)	91,335	100,327	71,842	94,505	76,841	-42,147	-
Profit before income tax (in EUR 000)	54,475	49,993	25,196	40,344	19,940	-110,279	-
Profit for the year (in EUR 000)	43,814	40,761	21,119	30,387	12,489	-104,620	-
Gross cash flow from operating activites (EBITDA) (in EUR 000)	162,046	176,773	167,296	170,087	158,146	108,745	68.8
Gross cash flow from operating activites before rental expenses (EBITDAR) (in EUR 000)	171,781	198,158	190,619	204,846	202,330	167,242	82.7
BALANCE SHEET							
Total assets (in EUR 000)	2,070,473	2,540,122	2,476,348	2,586,759	2,613,659	2,522,820	96.5
Equity (in EUR 000)	688,196	814,101	805,390	776,704	756,457	663,249	87.7
Net financial debt (in EUR 000)	749,439	958,881	986,966	949,081	1,091,145	1,008,034	92.4
INVESTMENT ACTIVITIES							
Capital expenditure (in EUR 000)	164,850	298,305	157,353	116,394	119,715	67,330	56.2
Long-term financial investments (in EUR 000)	49,221	15,104	1,801	0	2,248	9	0.4
EMPLOYEES							
Number of employees as at the end of the period	20,893	21,636	21,404	23,482	24,266	23,920	98.6
Number of employees based on hours worked	19,099	20,438	20,266	21,632	22,602	22,769	100.7
FINANCIAL INDICATORS							
Revenue per employee based on hours worked (in EUR 000)	128.0	132.5	130.4	128.6	127.0	126.2	99.3
Value added per employee per hours worked (in EUR 000)	22.9	22.8	22.0	21.4	22.5	20.4	90.6
Return on sales	1.8%	1.5%	0.8%	1.1%	0.4%	-3.6%	-
Return on equity	6.8%	5.6%	2.6%	3.9%	2.4%	-13.7%	-
Net financial debt / equity	1.09	1.18	1.23	1.19	1.44	1.52	105.4
Net financial debt / gross cash flow from operating activities (EBITDA)	4.62	5.42	5.90	5.58	6.90	9.27	134.4
Gross cash flow from operating activites (EBITDA) / revenue	6.6%	6.5%	6.3%	6.1%	5.5%	3.8%	68.7
Gross cash flow from operating activites before rental expenses (EBITDAR) / revenue	7.0%	7.3%	7.2%	7.4%	7.0%	5.8%	82.6
SHAREHOLDERS INFORMATION							
Market value per share as at the end of the period (in EUR)	335.0	158.1	153.2	157.7	147.0	114.0	77.6
Dividend per share (in EUR)	4.00	4.25	4.50	7.20	8.00	6.00	75.0
Earnings per share (in EUR)	11.8	10.9	5.7	8.2	3.3	-27.8	-
NUMBER OF COMPANIES IN THE GROUP							
Number of companies in the group as at December 31	16	20	23	26	26	36	138.5

MERCATOR GROUP PROFILE AND ORGANIZATION

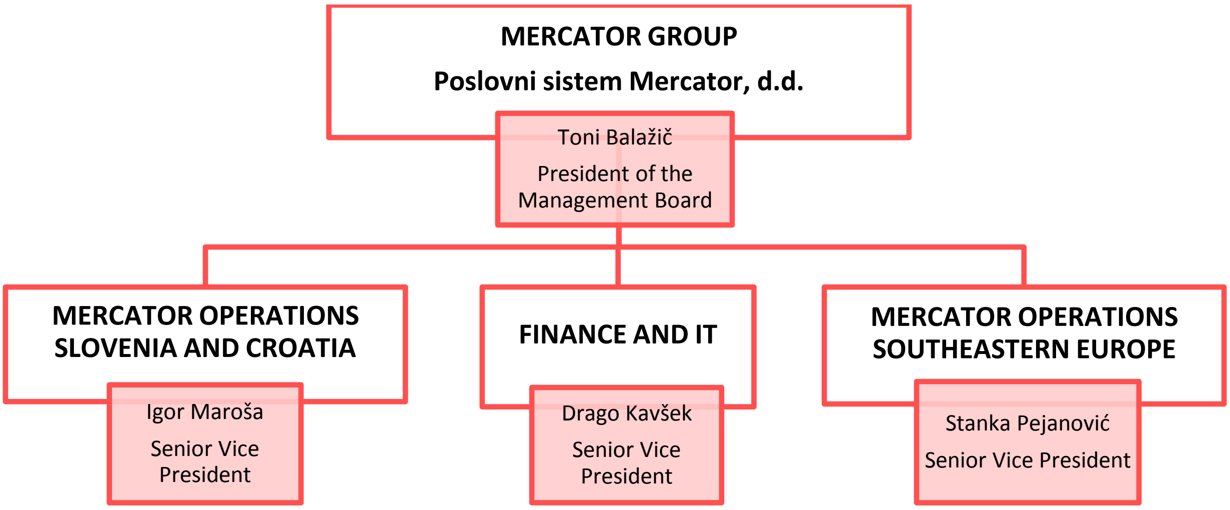
Mercator Group Profile

Mercator Group is one of the largest corporate groups in Slovenia and in the entire Southeastern European region. 19 of the companies comprising the Group are headquartered in Slovenia, while 17 more subsidiaries operate in the other seven markets of Southeastern Europe. Poslovni sistem Mercator, d.d., headquartered in Slovenia, is the parent company of the Group.

Poslovni sistem Mercator, d.d.

Telephone	+386 560 10 00
e-address	info@mercator.si
Website	www.mercator.si
Headquarter	Dunajska cesta 107, 1113 Ljubljana
Activity	Retail in non-specialized food retail outlets (G 47.110)
Registration number	5300231
VAT number	45884595
Company share capital as at December 31, 2012	EUR 157,128,514.53
Number of shares issued and paid-out as at December 31, 2012	3,765,361
Share listing	Ljubljana Stock Exchange, d.d., official market, prime market, symbol MELR

Organization and Composition of the Mercator Group



Following the appointment of the new Management Board, a revised organizational structure was put into place. It involves the following three areas: **Mercator operations Slovenia and Croatia, Mercator operations Southeastern Europe**, and **Finance and IT**. The new leaner organization will allow the Management Board to focus on the management of two groups of markets as it is set to maximize the efficiency of the marketing strategy and growth, and to optimize costs. Support functions will be managed centrally, which will improve their efficiency.

As at December 31, 2012, Mercator Group included the following :

MERCATOR GROUP

MERCATOR OPERATIONS SLOVENIA AND CROATIA

Poslovni sistem Mercator, d.d., Slovenia
Mercator - H, d.o.o., Croatia (99.9%)
M - Tehnika, d.d., Slovenia (100.0%)
- Mercator centar tehnike d.o.o. za trgovinu i usluge, Croatia (100.0%)

Mercator IP, d.o.o., Slovenia (100.0%)
M - Energija, d.o.o., Slovenia (100.0%)
M.COM, d.o.o., Slovenia (100.0%)*

MERCATOR REAL ESTATE

Mercator - Optima, d.o.o., Slovenia (100.0%)
M - nepremičnine, d.o.o., Slovenia (100.0%)
Argentum - A, d.o.o., Slovenia (100.0%)**
Argentum - B, d.o.o., Slovenia (100.0%)**
Argentum - C, d.o.o., Slovenia (100.0%)**
Argentum - D, d.o.o., Slovenia (100.0%)**
Argentum - E, d.o.o., Slovenia (100.0%)**
Argentum - F, d.o.o., Slovenia (100.0%)**
Argentum - G, d.o.o., Slovenia (100.0%)**
Argentum - H, d.o.o., Slovenia (100.0%)**
Argentum - I, d.o.o., Slovenia (100.0%)**
Investment Internacional, d.o.o.e.l., Macedonia (100.0%)*

MERCATOR OPERATIONS SOUTHEASTERN EUROPE

Mercator - S, d.o.o., Serbia (100.0%)
Mercator - BH, d.o.o., Bosnia and Herzegovina (100.0%)
M - BL, d.o.o., Bosnia and Herzegovina (100.0%)
Mercator - CG, d.o.o., Montenegro (100.0%)
Mercator - B, e.o.o.d., Bulgaria (100.0%)
Mercator - A, sh.p.k., Albania (100.0%)
Mercator Makedonija, d.o.o.e.l., Macedonia (100.0%)*
Mercator - K, l.l.c., Kosovo (100.0%)*

OTHER OPERATING ACTIVITIES

Intersport ISI, d.o.o., Slovenia (100.0%)
- Intersport S-ISI, d.o.o., Serbia (100.0%)
- Intersport H, d.o.o., Croatia (100.0%)
- Intersport BH, d.o.o., Bosnia and Herzegovina (100.0%)

Modiana, d.o.o., Slovenia (100.0%)
- Modiana, d.o.o., Serbia (100.0%)
- Modiana, d.o.o., Croatia (100.0%)
- Modiana, d.o.o., Bosnia and Herzegovina (100.0%)

Mercator - Emba, d.d., Slovenia (100.0%)

* The company has not yet commenced its business operations.
** Project-based real estate company which has not launched its activities yet.

Branch Offices
As at December 31, 2012, Mercator Group companies did not have any branch offices.

Other Organizations
The company Poslovni sistem Mercator, d.d., is the founder of the Mercator Humanitarian Foundation whose purpose is provision of humanitarian aid to Mercator employees.

MERCATOR GROUP ACTIVITIES

The primary and key activity of the Mercator Group is retail of fast-moving consumer goods. This core activity is extended with offer of supplementary services. Thus, we are looking to present to our customers a comprehensive offer that will fit their needs and desires.

Fast-moving consumer goods

Mercator Group has developed a dense and extensive retail network throughout Slovenia and other countries, providing high-quality offer to meet every customer's desires, tastes, and needs. We are working to bring our shopping centers, hypermarkets, supermarkets, smaller neighbourhood stores, Hura! discount stores, and the web store as close as possible to the customers, and to provide a pleasant shopping experience.

Home products

The M Tehnika (technical consumer goods), M Gradnja (construction) and M Pohištvo (furniture) stores offer products for home at favourable payment terms. The offer includes high-quality and reliable construction materials, modern furniture and equipment for every room in the home and office, modern home appliances and major appliances, and consumer electronics by globally renowned manufacturers. Offer of the M Tehnika web store is another step forward in the home product program.

Mercator Real Estate

Since the Mercator Group owns considerably more property than its competitors, real estate management is organized as a special business field. The fundamental tasks of the real estate field include optimum management of real estate, development of retail network, and improving the attractiveness of shopping centers.

Other operating activities

Mercator Group conducts additional business activities in order to deliver all-around offer for the customers. Intersport stores offer sportswear; Modiana stores offer clothing and other textile products. In addition, consumers are offered self-service petrol stations (Maxen), and tourist services of the M holidays agency. Mercator Group also includes the manufacturing company Mercator-Emba, d.d.

MAJOR EVENTS IN 2012

Retail network development

In 2012, we invested EUR 67.3 million in retail network development, while divestment amounted to EUR 6.8 million. The Group acquired 54 new units spanning 56,908 square meters, which includes real estate owned by Mercator and operating leases.

Changes in the composition of the Mercator Group

Along with the appointment of the new Management Board, a revised macro-organizational structure of the Mercator Group was put into place, which is effective from March 1, 2013. New organization will allow focusing on the management of two groups of markets within the fields Mercator Operations Slovenia and Croatia, and Mercator Operations Southeastern Europe. By managing two independent geographical units, we are planning to maximize our marketing strategy and growth, and to optimize our costs. Support functions will be managed centrally, which will make them more cost-efficient.

New organizational structure brings maximization of marketing strategy and growth, as well as cost rationalization.

On February 23, 2012, the agreement on strategic combination entered into force. Based on the agreement, the company Poslovni sistem Mercator, d.d., increased its shareholding in the company Vesna, trgovsko podjetje (trade company), d.d., Ljutomer, from 45 percent to 100 percent, thus acquiring seven stores in Northeastern Slovenia, which operated as Mercator franchise units to date. On August 23, 2012, the company was merged with Mercator, d.d.

Consistently with the activities of the monetization project, nine project real estate companies Argentum were founded in March 2012.

On March 16, 2012 the company Mercator centar tehnike, d.o.o. za trgovinu i usluge (Mercator Technical Consumer Goods Center, limited liability company for trade and services) was founded, which is a subsidiary of M - Tehnika, d.d. The technical consumer goods program, previously included in the company Mercator - H, d.o.o., was transferred to the newly incorporated company.

On December 31, 2012 the Group withdrew from the market of Albania. Sales units ceased to operate while the company Mercator - A, sh.p.k., continues to operate as an independent legal person. In the course of 2013, exit from Bulgarian market will be carried out as well.

Corporate governance

On March 29, 2012, the five-member Mercator Management Board at the time, consisting of Mr Žiga Debeljak, Ms Vera Aljančič Falež, Ms Melita Kolbezen, Ms Stanka Pejanović, and Mr Peter Zavrl submitted their resignation. Six new Supervisory Board members were appointed at the Shareholders Assembly on March 30, 2012. The New Supervisory Board held their first session on April 10, 2012. At the first session, the new Supervisory Board appointed Mr Matej Lahovnik as the new Supervisory Board chairman. The Board also appointed new members of the Audit Committee and Human Resource Committee. The Supervisory Board appointed a new Mercator, d.d., Management Board, assigning Mr Toni Balažič as the President of the Management Board; Mr Drago Kavšek as the Senior Vice President in charge of finance and IT; Ms Stanka Pejanović as Senior Vice President in charge of Mercator operations Southeastern Europe; and Mr Igor Maroša as the Senior Vice President in charge of Mercator operations Slovenia and Croatia. New Management Board members were appointed for a term of five years.

In February, the Management Board of the company Mercator, d.d., presented the Group performance and operations in 2011, and the plans for 2012. At the press conference in August, the new Management Board presented the results of the first half of the year and the measures and targets for the future. On October 18, 2012, the company Supervisory Board confirmed the Mercator Group strategy as developed by the new Management Board.

A Consortium of shareholders of the company Mercator, d.d., representing 53.18 percent of the share capital of the company Mercator, d.d., and the company Mercator, d.d., have entered into a Memorandum on Cooperation. Memorandum sets out the conditions, scope and duration of cooperation between the Consortium of shareholders and the company in the sale process of Mercator shares.

Corporate activities

On April 24, 2012, Mercator took part in the **7th Day of Slovenian Capital Market**, organized by the Ljubljana Stock Exchange in cooperation with the KDD – Central Securities Clearing Corporation, and event partners Alta Invest, d.d., and NLB, d.d. In addition to the presentations of enterprises, the event involved individual meetings intended exclusively for portfolio investors.

In order to boost international recognition of its shares, the company Poslovni sistem Mercator, d.d., published in 2012 the proxy authorization and Shareholders Assembly convocation in the **EuroVote** system. The project was established in order to promote and facilitate international voting through proxies in the European Union, via the Euroshareholders web platform.

Awards received

Mercator won the first prize for the best international internal communication strategy, for its project "corporate value cube".

In the best Annual Report contest held each year by the Finance daily paper, the company **Poslovni sistem Mercator, d.d.**, received the award for the **Best Annual Report in communication** for the year 2011. The award is a result of carefully thought-out decisions adopted in order to offer our users simple access to information and processing thereof. In addition, the jury was also impressed by the appealing and modern Annual Report design.

Mercator's subsidiary **Mercator IP, d.o.o.,** won the **Best Annual Report among small and medium enterprises** award for the year 2011.

On November 7, 2012, FEIEA, the Federation of European Business Communicators Associations announced at a festive ceremony in Zurich the winners of the FEIEA Grand Prix 2012 contest for the **best internal communication practices in Europe**. 103 entries from 10 European countries competed in 15 categories: from printed and electronic media to internal communication strategies and events. The jury chose three best practices in each category. **Mercator won the first prize in the category the best international strategy of internal communication** for the project of the cube, or dice, carrying the message of corporate values.

At the 12th competition of bread, pastry, and pasta, held by the Bakery Section of the Chamber of Agricultural and Food Companies with the Chamber of Commerce and Industry of Slovenia, Mercator's own bakery **Pekarna Grosuplje received the highest possible rating for all nine zero-additive products submitted**.

At the POMP Forum 2012, an international content marketing conference, The "**Maxi magazin**", a Maxi department store newsletter, **received a special achievements award for development of content marketing in 2012**.

Maxim restaurant was awarded the **Ljubljana Quality seal for 2012** as the best rated high-end restaurant. The choice of Ljubljana quality is a trademark denoting attainment of high standards of offer, quality of service, and maintenance of HoReCa outlets. The restaurant boasting the LQ seal has a comprehensive offer that includes the best food, service, and ambience. The seal is effective for two years from the day it is awarded.

CORPORATE GOVERNANCE STATEMENT

Pursuant to Article 70, Paragraph 5 of the Companies Act (ZGD-1), Business Report of the company Poslovni sistem Mercator, d.d., also includes a Corporate Governance Statement.

Reference to the Corporate Governance Code

The governance of the company Poslovni sistem Mercator, d.d., is based on legal provisions, sound business practice, and the principles of the Corporate Governance Code. The Corporate Governance Code (Official Journal RS No. 118/2005, dated December 17, 2005, changed and amended on February 5, 2007, revised and adopted on December 8, 2009) – hereinafter: the Code, is available in Slovenian and English at the website of the Ljubljana Stock Exchange, d.d., at www.ljse.si. The company's decision to commit to the provisions of the Code is voluntary.

Management and Supervisory Board of the company Poslovni sistem Mercator, d.d., headquartered at Dunajska cesta 107, Ljubljana, hereby submit this statement of compliance with the Code, which is also a constituent part of the 2012 Annual Report. It is available at company website at www.mercator.si.

Compliance with the provisions of the Code

Management Board and Supervisory Board of the company Poslovni sistem Mercator, d.d., have reviewed the corporate governance at the company Poslovni sistem Mercator, d.d., and the Mercator Group, and the compliance thereof with the Code, and prepared a new statement which reflects the actual situation of corporate governance at the company Poslovni sistem Mercator, d.d., and the Mercator Group.

It was found that corporate governance at the company Poslovni sistem Mercator, d.d., and the Mercator Group complies with the provisions of the Corporate Governance Code, with particular deviations explained below.

Relations with shareholders

<u>Recommendation 4.2:</u> Given the fact that major shareholders communicate their investment plans on own initiative, the company did not invite them separately to publicly disclose their management policies with regard to their investment in this publicly traded stock corporation.

<u>Recommendation 5.2:</u> The company publicly announced on its website all information about lodging proxies for voting at particular Shareholders Assemblies; in addition, each shareholder was informed individually in this regard. However, the company did not announce on its website the information on the cost of organized lodging of voting proxies at particular Shareholders assemblies, although it did make sure the most competitive provider of these services was hired.

Supervisory Board

<u>Recommendation 7.1:</u> Some Supervisory Board members have not produced documentation to prove their specialized professional or expert competencies for Supervisory Board membership. Nevertheless, they qualify for such engagement due to professional competencies or experience.

<u>Recommendation 8:</u> All Supervisory Board members have signed a special statement specifying their position on meeting each of the independence criteria. However, the company did not announce the signed statements on its website; the statements are deposited at the company headquarters.

Mercator shall continue to observe the recommendations of the Code in the future, looking to implement as far as possible the non-binding recommendations of the Code and thus to improve its corporate governance system.

Description of key characteristics of internal control and risk management at the company, with regard to the financial reporting process

In a rapidly changing business environment, efficient and successful business decision-making requires quality and timely information. Provision of financial information is the responsibility of the company Management Board. Risks occurring in the process of preparation and compilation of such information are managed in the following ways:

- clear and concise accounting practices and their strict implementation;

- completely synchronized accounting policy throughout the entire Group;
- efficient organization of the accounting function at each company, as well as at the Mercator Group level;
- comprehensive and extensive disclosures and explanations;
- timely preparation, detailed treatment, and suitable concept in terms of contents and substance in statements relevant for business decision-making;
- preparation of financial statements in line with the International Financial Reporting Standards (IFRS);
- regular internal and external audits and reviews of business processes and operations.

Mercator Group companies compile their financial statements pursuant to the International Financial Reporting Standards (IFRS), making sure that the financial position, income, and cash flows are presented fairly and consistently with the actual effects of business events.

Many internal controls have been put into place in order to support and facilitate these activities. The purpose of internal controls in accounting is to manage the risks pertaining principally to the following:

- credibility of accounting information based on valid and credible bookkeeping documents, and evidence of the existence of business events, complete with a clear presentation of all information relevant for correct bookkeeping of such events;
- accuracy of financial data which is appropriately reviewed before announcement; controls are conducted at several levels by comparing the data of analytic bookkeeping to the data in the bookkeeping documents, as well as to the data of business partners or actual physical status of assets, and bringing into line the analytical accounting and the main ledger;
- completeness and timeliness of financial information, provided by uniform accounting policies and precisely defined procedures and recording deadlines as laid down in the Accounting manual of the Mercator Group, and in other internal acts of the Group companies; also important is appropriate delineation of tasks and responsibilities.

The information system plays a vital role in the provision of quality accounting information from the aspect of the use of modern technology. Most Mercator Group companies employ SAP as the main IT system. It is fittingly integrated with other IT solutions at the Group companies. Operation of the SAP system and the internal controls integrated therein are checked annually in cooperation with authorized third-party service providers.

All this, however, is only possible with highly professional, meticulous, and persistent employees complying with the relevant legislation and sharing Mercator's values. Therefore, a lot of care is devoted to their regular education. We provide both internal and third-party professional education, as well as training to acquire the "soft" skills.

Audit

Pursuant to the Companies Act, audit of financial statements is mandatory for Mercator Group companies. The purpose of the audit is to increase the level of trust among the users of financial information. The auditor applies appropriate audit procedures and methods to review the financial statements and passes an opinion as to whether they are compiled in compliance with the appropriate framework of financial reporting in all relevant aspects.

External audit

At the 18th regular Shareholders Assembly, company shareholders appointed the auditing company KPMG Slovenija, podjetje za revidiranje, d.o.o., as the auditor for the company Mercator, d.d., and the Mercator Group for the year 2012 as well. Since this company was selected as the company auditor for the sixth year, the key auditing partner was changed, pursuant to the Corporate Governance Code.

Auditing company KPMG Slovenija, podjetje za revidiranje, d.o.o., employs the most recent audit methodology as laid down in the KPMG Audit Manual (KAM) which is prepared to comply with the latest national and international auditing standards, as well as to support and improve the quality of the audit and contribute to its efficiency.

Internal audit

In addition to the Management Board, Supervisory Board, and independent auditor, internal audit is one of the pillars of corporate governance. Internal audit is an independent and non-biased activity engaged in providing assurance and recommendations. Its purpose is to boost the benefits and improve the operations and performance of all Mercator Group companies. It aids the companies in the pursuit of their goals by promoting carefully thought out and neat method of evaluation of internal controls and risks, and improvement of the success of risk management processes. It also offers aid to Audit Committee members by providing assurance regarding risk management, effectiveness of internal controls, and managerial processes within individual companies.

Activities of Mercator Group internal audit are compliant with the International Standards of Professional Conduct in internal auditing, Code of Professional Ethics for Internal Auditors, and the Code of Internal Auditing Principles.

On the basis of conclusions of external assessment, the Audit Committee of the Supervisory Board of the company Poslovni sistem Mercator, d.d., has supported the change in the organizational placement of internal audit under the Management Board of the company.

Assurances provided by internal audit to management teams of individual companies and to the Supervisory Board are based on regular and extraordinary internal audits. In 2012, internal audit conducted 29 regular and 12 extraordinary internal audits at 18 Mercator Group companies. The following major fields or processes were reviewed and audited: risk management, management of trade receivables and discounts granted to wholesale customers, price calculation process, goods import procedures, transition to net-net pricing system, protection of personal information in operations involving the Pika card, procurement of non-trade goods and services, travel expense accounting, management of fleet of personal vehicles, and personal income tax accounting.

Audit Committee

Audit Committee of the Supervisory Board of the company Poslovni sistem Mercator, d.d., has been in operation with varying membership since 2008.
Pursuant to the adopted Rules of Procedure, the Committee holds at least four sessions each year. Pursuant to Article 280 of the Companies Act, it has the following major responsibilities:

- controlling the validity and accuracy of financial information reported by the company;
- controlling the operation of the risk management system, internal audit, and the system of internal controls;
- evaluating the composition of the Annual Report, including the proposal for the Supervisory Board;
- taking part in defining the main fields of auditing;
- taking part in the selection of an independent third-party auditor and preparing the agreement to be signed between the auditor and the company;
- supervising the independence, neutrality, and efficiency of independent third-party auditors;
- supervising the nature and scope of non-auditing services.

The Audit Committee reports on their work to the Supervisory Board.

Horizontal Monitoring

On October 5, 2010, the company Mercator, d.d., signed an agreement with the Tax Administration of the Republic of Slovenia to take part in the pilot project of Horizontal Monitoring. Cooperation was initially agreed upon for the years 2011 and 2012. Late in 2012, an annex was signed to extend the cooperation to the year 2013.

In 2011 and 2012, operation of internal controls was reviewed with regard to accounting of value-added tax, personal taxes, and corporate income tax. The Tax Administration found that the system of internal controls in place at the company works well in the said fields, and proposed some further improvements. Hence, participation in the Horizontal Monitoring project leads to higher certainty in terms of taxation, particularly due to partnership relationship and constant open cooperation with the Tax Administration.

Restriction of voting rights

Up to May 26, 2012, the decision No. 0600-9/2010-59 dated September 23, 2010, issued by the Securities Market Agency, was in force. It prohibited in 2012 exercising the voting rights based on all shares of the target company Poslovni sistem Mercator, d.d., and MELR shares, to NLB, d.d., Banka Celje, Abanka Vipa, d.d., Gorenjska banka, d.d., NKBM, d.d., and Banka Koper, d.d., due to concerted action and for exceeding the takeover threshold. The said decision expired on May 26, 2012 when the Act Amending the Takeovers Act was enacted, specifying takeover threshold at a higher shareholding of the target company than that held by the above banks.

Composition of major holders of company securities as at December 31, 2012

	Major Shareholders	Country	Number of shares	Share
1	Pivovarna Union, d.d.	Slovenia	464,390	12.33%
2	NLB d.d.	Slovenia	404,832	10.75%
3	Societe Generale-Splitska banka, d.d.	Croatia	381,658	10.14%
4	Pivovarna Laško, d.d.	Slovenia	317,498	8.43%
5	UniCredit banka Slovenija, d.d.	Slovenia	301,437	8.01%
6	Nova KBM d.d.	Slovenia	197,274	5.24%
7	HYPO Alpe-Adria bank d.d.	Croatia	158,797	4.22%
8	GB d.d., Kranj	Slovenia	142,920	3.80%
9	Prvi faktor - faktoring, d.o.o., Belgrade	Serbia	125,963	3.35%
10	Radenska, d.d.	Slovenia	96,952	2.57%
		Total	**2,591,721**	**68.84%**

Company rules on appointment and replacement of members of managerial and supervisory bodies and changes to the Articles of Association

The company Poslovni sistem Mercator, d.d., is represented by the Management Board. The Management Board consists of four members. Its purpose is to diligently and responsibly pursue the goals laid out, in compliance with the Corporate Governance Code. 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. Based on the Supervisory Board resolution, President of the Management Board and Senior Vice Presidents were appointed for a five-year term, starting from June 1, 2012 for the President and June 19, 2012 for the Senior Vice Presidents. All Management Board members of the company Poslovni sistem Mercator, d.d., signed their respective fixed-term employment agreements with the company for a period of five years, which is consistent with the duration of their terms.

The fundamental function of the Supervisory Board is to supervise the management of company affairs. Pursuant to the corporate governance code, Supervisory Board member are independent in their work and decision-making. The Supervisory Board includes members who represent the interests of the shareholders and are appointed by the Shareholders Assembly, and members who represent the interests of the employees and are appointed pursuant to the Worker Participation in Management Act, by the company Works Council.

Changes to the Articles of Association are adopted by the Shareholders Assembly with a three-quarter majority of the represented share capital.

Information on the Shareholders Assembly operations and the rights of shareholders and the manner of their enforcement

Shareholders Assembly is the superior body of governance through which the shareholders assert their rights with regard to the company affairs. The company Poslovni sistem Mercator, d.d., is committed to full compliance with the principle of equal treatment of shareholders, allowing them to exercise their legal or statutory rights. All shareholders shall have equal voting rights.

As a rule, Company Management Board shall convene the Shareholders Assembly of Poslovni sistem Mercator, d.d., once per year. The convocation shall be announced at least 30 days before the Assembly meeting. The convocation of the Assembly shall be 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.

In addition to the location and time of the Assembly, the convocation, or announcement defines the conditions for taking part in the assembly and asserting the voting right, as well as the agenda and proposed resolutions. A shareholder or a proxy may assert the voting right at the Assembly by presenting a written authorization. Convocation of the Assembly, agenda, proposed resolutions with the relevant explanations, and the Assembly resolutions, are also announced on the company website at www.mercator.si.

On March 30, 2012, 18th regular Shareholders Assembly took place with 66.69 percent of total shares with voting rights present. The Assembly included a presentation of the Annual Report and the Supervisory Board Report on the Annual Report Audit for the fiscal year 2011, as well as information on the compensation paid to members of managerial and supervisory bodies. The Assembly voted on the allocation of distributable profit for 2011 and dividend payment, and granted discharge to the Management Board and Supervisory Board. Furthermore, the Assembly appointed the certified auditing company for the year 2012 and a special auditor to review the management of particular transactions. The Assembly also recalled previous Supervisory Board members (representatives of capital) and appointed new ones.

Managerial and supervisory bodies

MANAGEMENT BOARD:

President of the Management Board – Toni Balažič

Education:

- MBA, BA Economics.

Fields of responsibility:

- coordinating the work of the Management Board of Poslovni sistem Mercator, d.d., and the Mercator Group,
- strategic marketing,
- public relations,
- human resources, legal affairs, and organization,
- real estate management.

Senior Vice President in charge of Mercator operations Southeastern Europe – Stanka Pejanović

Education:

- MScBA, BA Economics.

Fields of responsibility:

- management of trade operations in the markets of Southeastern Europe: Serbia, Bosnia and Herzegovina, Montenegro, Albania, and Bulgaria,
- management of other fields subject to authorization by the President of the Management Board.

Senior Vice President in charge of finance and IT – Drago Kavšek

Education:

- BA Economics.

Fields of responsibility:

- finance, controlling, accounting, and internal audit,
- IT and telecommunication,
- management of other fields subject to authorization by the President of the Management Board.

Senior Vice President in charge of Mercator operations Slovenia and Croatia – Igor Maroša

Education:

- MSc, BA Economics

Fields of responsibility:

- management of trade operations in Slovenia and in Croatia,
- managing other fields subject to authorization by the President of the Management Board.

From left to right: Stanka Pejanović, Drago Kavšek, Toni Balažič and Igor Maroša.

SUPERVISORY BOARD MEMBERS:

Supervisory Board Chairman – Matej Lahovnik

- Education: PhD in management and organization.
- Employment: Faculty of Economics, University of Ljubljana; assistant professor.

Supervisory Board Members Representing Shareholders

Rok Rozman, Deputy Chairman

- Education: Master of Laws (LL.M.).
- Employment: UniCredit Banka Slovenija, d.d.; authorized representative/officer with statutory power (procurator).

Boris Galić

- Education: BA Economics.
- Employment: Allianz Zagreb, d.d.; management board president.

Zdenko Podlesnik

- Education: BA Economics.
- Employment: CBH, d.o.o., Celje; managing director.

Marjeta Zevnik

- Education: Bachelor of Laws (LL.B.).
- Employment: Pivovarna Laško, d.d., Laško; Management Board member in charge of legal affairs, HRM, and general affairs.

Supervisory Board Members Representing Employees

Mateja Širec

- Education: BA Sociology.
- Employment: Head of section at Poslovni sistem Mercator, d.d.

Ivan Valand

- Education: BA Economics.
- Employment: Head of Hypermarket II at Poslovni sistem Mercator, d.d.

Sandi Leban

- Education: BA Economics.
- Employment: security expert in the territory of western Slovenia at Poslovni sistem Mercator, d.d.

Information on activities and composition of the Audit Committee

The Audit Committee of the Supervisory Board of the company Poslovni sistem Mercator, d.d., operates pursuant to the provisions of the Companies Act. The activities of the Audit Committee are aimed at further improvement of performance of the supervisory function at the company.

A new Supervisory Board was appointed in April 2012; as a result, new Audit Committee was also appointed.

Until April 10, 2012, the Audit Committee of the Supervisory Board of the company Poslovni sistem Mercator, d.d., had the following three members: chairwoman Jadranka Dakič (Supervisory Board member) and two members: Jože Cvetek (Supervisory Board member) and Peter Ribarič, MSc, (independent expert on accounting and auditing).

The new Supervisory Board appointed a four-member Audit Committee. Its members include chairwoman Marjeta Zevnik (Supervisory Board member) and three members: Rok Rozman, MSc, (Supervisory Board member), and Sergeja Slapničar, PhD, and Aleksander Igličar, MSc, (both independent experts on accounting and auditing).

The Supervisory Board also specified their compensation which shall amount to one half of the monthly compensation paid to the Supervisory Board chairperson or members, respectively. Audit Committee members receive for the performance of their tasks and duties monthly payments, as well as session fees. Monthly compensation paid to the Audit Committee chairperson amounts to EUR 1,250.00 gross; other members receive EUR 750.00 gross per month each. Session fee amounted to EUR 200.00 net for the Audit Committee members and EUR 350.00 net for the chairwoman. All amounts remained the same relative to the year 2011.

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, optimum 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 Management Board performs the function of company Assembly; alternatively, the parent company 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. None of the employees receives additional payment for performing these tasks in the supervisory bodies of subsidiaries.

Management Responsibility Statement

The company Management Board is responsible for the compilation of the Annual Report for the company Poslovni sistem Mercator, d.d., and the Mercator Group for the year 2012, including all relevant financial statements which, to the best knowledge of the Management Board, present truly and fairly the development and performance of company operations and the company's financial position, including the description of all significant types of risks to which the company, any other companies included in the consolidation, or the Group as a whole, are exposed.

The Management Board confirms that the financial statements were compiled by applying duly and consistently the relevant accounting policies; that the accounting estimates were made on the principles of fair value, prudence and sound management; and that financial statements represent a true and fair view of the company's financial position, and of the results of its operations in 2012.

The Management Board shall also be responsible for appropriate and accurate accounting, and adoption of relevant measures to protect its property and other assets. The Management Board hereby confirms that the financial statements, including all and any notes, are compiled based on the going concern assumption and in compliance with relevant legislation and International Financial Reporting Standards as adopted by the European Union.

The company Management Board hereby adopts and confirms the Annual Report for the company Poslovni sistem Mercator, d.d., and the Mercator Group for the year 2012.

Ljubljana, February 27, 2013

Toni Balažič
President of the Management Board

Stanka Pejanović
Senior Vice President

Drago Kavšek
Senior Vice President

Igor Maroša
Senior Vice President

MERCATOR GROUP NEW BUSINESS STRATEGY

Vision

Mercator will be the largest, the most successful and the most efficient retailer in the region.

Mission

- A satisfied customer recognizes us as the best retailer that offers everything a discount store can offer, and much more.
- Employees with **smiles on their faces and sparkles in their eyes** are our key competitive advantage. They will be able to develop their potential in a stable environment.
- We are striving towards a **stable ownership structure** that will support the company development based on merit and results.
- Mercator is striving to win the **confidence of all stakeholders**.

Principles of corporate governance

Our work shall be:

Motivated

Elementarily simple

Rational

Common goal oriented

Ambitious

Thorough

Oriented on profitability and development

Rapturous

Four pillars of the strategy and goals for the medium-term period 2013-2016

Focus

Consumer: restore confidence and satisfaction ***Region: focus on countries with potential for growth and short-term profitability*** ***Activities: core activity***	In 2013, we shall exit the market of Bulgaria. In addition, restructuring of operations in Croatia is also a major project. Regarding customer satisfaction we shall focus even more actively on understanding the needs of local customers and improvement of the customer loyalty program through stabilization and growth of trade operations in Slovenia. In addition, we shall improve the price perception and elevate the level of services. In order to increase the focus on Mercator Group's core activity, programs Tehnika (technical consumer goods), Modiana (clothing and other textile), and M Energija (energy) will be intensively restructured.

Optimization

Simplifying the organization and processes ***Reaching the target productivity*** ***Optimization of all types of costs and expenses*** ***Invest a part of the savings into the market and the employees*** ***Financial stability***	In 2013, we shall reorganize, simplify, and centralize the business functions to optimize the processes, cut fixed costs, and pursue target productivity. By 2016, we shall optimize the entire supply chain in logistics; this will include reaping synergy effects with Croatia. Activities of the companies Intersport, Modiana, and M Tehnika will be merged with Mercator companies in individual markets. Level of service at the stores will be elevated and the system of employment rewards will be upgraded to promote customer and employee satisfaction. The company Mercator, d.d., has already developed a platform for fast revival of the monetization process which will be carried out once a stable ownership structure is secured and when the situation in the market improves. Decision on the financial restructuring method to be employed at Mercator Group will be made in the first half of 2013.

Profitability

We have to guarantee profitable operations ***Adequate returns for the shareholders***	Higher profit margins, resulting in higher profit, will be attained by establishing global supply and sourcing, consolidation of suppliers, and improvement in category management; this, however, will not be reflected in an increase of product prices. We shall improve our operations by reaping the synergies between Slovenia and Croatia and by optimizing our distribution network. We shall increase the value of capital and restructure the financing sources by deleveraging.

Growth

Size matters in our industry. Therefore, we must continue to grow, but largely through organic growth, with only targeted smaller takeovers.	Organic growth will be attained by targeted management of customer segments, product categories, and store formats. This will allow us to reverse the trend of declining market shares in the markets of Slovenia and Croatia, and to continue the expansion of our market shares in other markets of Southeastern Europe. Investments with the largest potential for growth and development will be

managed with higher priority.
We shall continue to grow through mergers and acquisitions, particularly of stores of smaller formats, and particularly those acquisitions that involve minimum investment and large potential for growth and synergy effects.

Activities completed in 2012 and early in 2013

Focus

By implementing the right marketing measures, we succeeded despite the harsh economic environment in **stopping the decline of market shares in Slovenia and Croatia, while our market share in Serbia increased.**
Consumers are at the heart of our operations. Marketing activities are continuously adjusted to their needs in order to **boost consumer confidence and satisfaction**. We introduced several projects, including **Good Price** (Dobra cena), **Mercator Market** (Mercatorjeva tržnica), and the project **Locally produced** (Iz domačih krajev) by which we have built a perception of a retailer with strong integration into the local environment. On February 1, we presented our customers our **revised Pika card customer loyalty program** which will include more special offers and immediate discounts for the Pika card holders.
We are focused on **optimization or retail unit operations** and on restructuring and revival programs at underperforming companies.
At the end of year 2012 we **exited from the market of Albania, exit from the market of Bulgaria** is planned for year 2013.

Optimization

Measures to rationalize our operations and correct and consistent implementation of the adopted cost control measures have resulted in **savings of EUR 10 million** in the second half of 2012.
Measures in financing allowed us to **reduce our debt by EUR 90 million**; effective working capital management led to its **decrease by EUR 135 million**, which released additional financial assets previously tied up in working capital.
A **new organizational structure** was put into place, which includes central management of support functions; this, in turn, will improve their efficiency.
We increased our **focus on smaller formats** of supermarkets and neighbourhood stores; the Refreshment of FMCG Program project involved **refurbishment of 24 supermarkets in Slovenia and 8 supermarkets in Croatia, and refresh an offer in more than 80 smaller stores in Slovenia**.
We adopted the strategy of **gradual reduction of retail area under the Getro brand in order to improve retail area productivity.**

Profitability

The project of **foreign exchange risk hedging** is currently in progress, aiming to minimize unexpected effects regarding negative currency translation differences.
Action plans were prepared for reaping the synergies between Slovenia and Croatia in the fields of **cutting of administrative expenses, efficiency of administrative services and departments, joint purchasing policy, and optimization of logistics capacities**.
Category management was linked to two fields; store formats and customer segments. This will allow us to implement a systematic, comprehensive, and more cost-efficient approach aimed at our target levels for profit margin and profits.
The share of sale of private label products has been continuously rising. In 2012, we saw a **14-percent increase in the share of private label in overall sales** Group-wide.

Growth

To date, Mercator retains the position of the only Slovenian traditional retailer that also offers FMCG through a web store. This channel is being developed by **introducing the new Click&Collect service and by renovating the user interface and offer through the web store**.
In international markets, we have seen **Mercator's market share rise**; in Slovenia and Croatia, we have succeeded in stopping its decline.
In the second half of 2012, we **stopped the progress of non-essential investments** and continued to acquire new retail area especially through lease.
Consistently with the adopted medium-term strategy for the period 2013-2016, we optimized our investments in the entire year 2012. As a result, investments amounted to a total of **EUR 67 million**, which is **44 percent less** than in the year before. In addition, our **divestments totalled at EUR 6.8 million.**

BUSINESS REPORT

SALES AND MARKETING

Sales

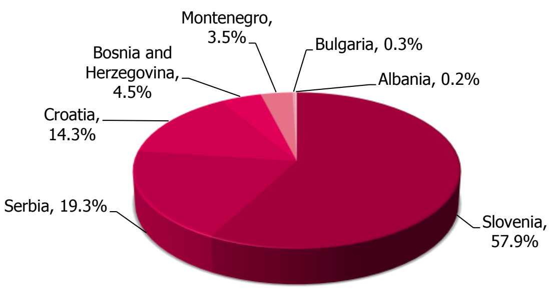
In 2012, trade industry was pressured by harsh economic conditions. Economic growth was low or even negative in all markets of Mercator's operations; this was paired with high unemployment rates which continue to rise. As a result, purchasing power is low and consumers are conservative and rational in their shopping behaviour. Despite these negative factors, Mercator Group generated EUR 2,873 million of revenue by effective marketing and cost-cutting activities.

Mercator Group revenue remained at the same level as in the year before; revenue growth in foreign markets reached nearly 4%.

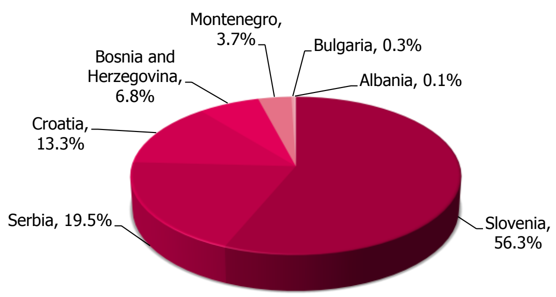
Relative to 2011, Mercator Group revenue remained virtually the same in 2012. In Slovenia, revenue dropped by 2.6 percent while in foreign markets, we saw revenue growth of 3.7 percent.

Mercator Group revenue by geographical segments:

2011

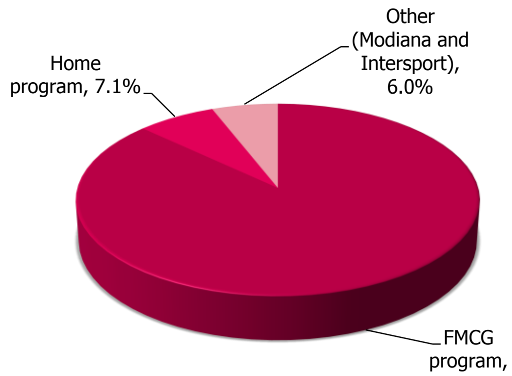


2012

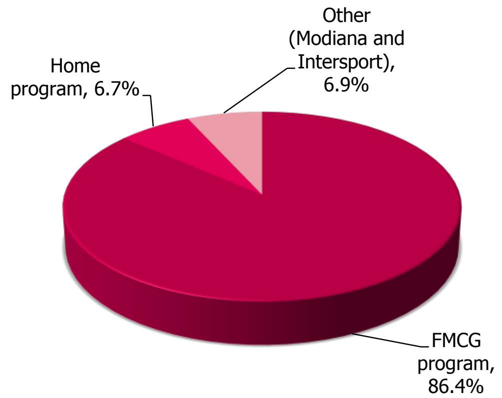


Mercator Group revenue from trade operations by programs:

2011

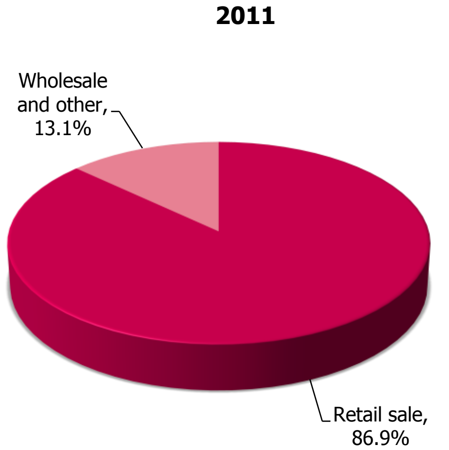


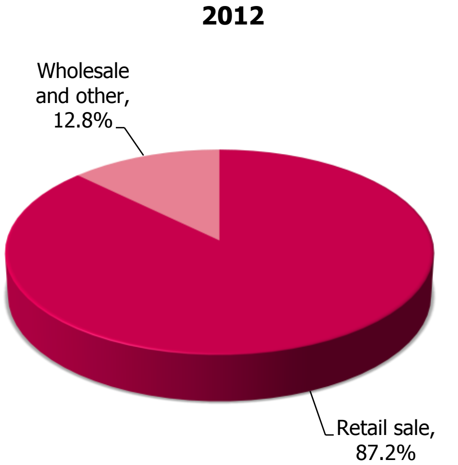
2012



In 2012, the majority of Mercator Group trade revenue resulted from sales of fast-moving consumer goods as they accounted for 86.4 percent of total net sales revenues; revenue from other specialized programs amounted to 13.6 percent.

Mercator Group revenue by type of sale:





In 2012, Mercator Group retail operations generated 87.2 percent of the Group's revenue from sales of goods and material, while the remaining 12.8 percent was generated in wholesale. The share of wholesale in total sales dropped by 0.3 percentage point.

Store formats, customer segments, and category management

We have designed a three-dimensional approach to category management, customer segment management, and store format and services management.

At Mercator, we are aware that in a rapidly changing environment challenged by negative effects of the economic crisis, the right and all-around approach to our customers is essential. Mercator's market presence is based on the reputation of a retailer focused on meeting the needs of a wide range of customers through an extensive retail network comprising stores of various formats. Pursuant to the new strategy, we launched the activities geared towards adjustment of offer and services in a way that will please all segments of our customers. To this end, we designed a three-dimensional approach that brings together the key areas: customer segment management, store format and services management, and category management.

Store Formats

Currently, Mercator Group's retail units are present in seven markets of different economic maturity. This requires adjusting our operations to the needs of the customers in each market. To this end, Mercator has put in place a multi-level strategy of store brands and a multi-format strategy with a broad range of store formats. These are intended to cater to major, previously planned shopping sessions, as well as minor, daily or occasional shopping for fast-moving consumer goods, technical consumer goods, cosmetics, sportswear, and tourist services.

Store formats by country and store brands

	STORE FORMAT	STORE BRAND	SLO	SRB	CRO	BiH	MNE	BG	ALB
FMCG	Hypermarkets	Mercator	■	■	■	■	■		■
		RODA		■			■	■	
		GETRO			■				
	Supermarkets	Mercator	■		■	■	■		
		RODA		■			■	■	
		GETRO			■				
		MARKETI za korpu VIŠE...				■			
	Neighbourhood, convenience and comfort stores	Mercator	■		■	■	■		
		RODA		■			■	■	
		GETRO			■				
		MARKETI za korpu VIŠE...				■			
	Cash&Carry	Mercator	■						
		RODA		■			■		
		GETRO			■				
	Franchise stores	Mercator	■	■	■				
Home products, textile and cosmetics, sportswear and other operating activities	Home and furniture program	Mercator	■	■	■				
		RODA		■			■		
	Sports program	INTERSPORT	■	■	■	■	■		■
	Clothing program	MODIANA	■	■	■	■	■		
	Drugstores and perfumeries	BEAUTIQUE	■	■		■			
	M holidays	HOLIDAYS	■						
	Maxen	MAXEN MAXIMALNA ENERGIJA	■						

Development of New Store Concepts

Social and demographic trends related to ageing of the population and changes in consumers' eating habits, **technological trends** like expansion of web businesses and development of new technologies that allow streamlining the shopping process, as well as **economic trends** (recession, market saturation, rising prices etc.) affect the shopping behaviour of the customers. Higher customer price sensitivity is manifest in lower value of the average shopping basket and lower frequency of shopping sessions as consumers distribute their shopping to several retailers and store formats, avoid longer drives when planning shopping trips, shop less impulsively, tend to be more rational when buying non-alimentary products of higher value etc.

In order to adjust to the customers as much as possible and offer them the most at a good price, Mercator launched in 2012 the development of new store format strategies based on which the entire marketing mix will be revised in the coming years in order to adapt it to particular target segments of the customers, and to their shopping intents and needs.

Hypermarkets

In 2012, we opened two new hypermarkets (HM Nova Gorica mesto and HM Novo mesto Bršljin), which employ a new and modern sales concept to respond to the shopping trends and provide a pleasant shopping experience for our customers.
The offer of these hypermarkets brings fresh produce to the fore of Mercator's offer. These products are offered at the entrance to the store. Another novelty in the offer is the "Minute" department located directly at the entrance into the store, which allows the customers to quickly and simply, from the walkway, purchase freshly prepared food suitable for immediate consumption.

In Serbia, HM Belgrade was reopened in September after a thorough refurbishment and redesign. The concept of each department has been developed to emphasize the visual elements (lighting, comprehensive visual identity of departments, labelling, equipment, technologies, extras etc.). Fresh program departments are combined to evoke the feel of a marketplace and the layout with a varied shopping walkway highlights particular departments of target categories that are of particular importance for Mercator.

Neighbourhood stores

Smaller neighbourhood stores are a competitive advantage for Mercator in the changing market conditions, owing to their good locations and wide regional coverage. Therefore, Mercator launched a campaign to reposition this store format in order to maintain and consolidate the position of the best neighbour in every neighbourhood, one that is "always there, caring, friendly, and involved in the local community". We wish to contribute to the benefit of the neighbourhood and our customers by offering excellent fresh program and innovative ideas for the mix of products and services that will make our customers' lives easier.

Neighbourhood stores provide a competitive edge for Mercator; moreover, successful adjustment of the retail network to the market trends also relies on convenience stores and comfort stores.

Convenience stores

As an innovative retailer that keeps up to date with the modern market trends, Mercator actively approached the development of the convenience store format. The offer at this format is adjusted to each particular micro location and its main mission is to afford customers in a hurry to do their shopping quickly and to choose from a varied range of ready-made products suitable for immediate consumption or use (quick occasional shopping).

Composition of retail units as at December 31, 2012

COUNTRY	SLOVENIA	SERBIA		CROATIA		BOSNIA AND HERZEGOVINA		MONTENEGRO		ALBANIA	BULGARIA	MERCATOR GROUP		
Banner		Mercator	Roda	Mercator	Getro	Mercator	Drvopromet	Mercator	Roda	Mercator	Roda			
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	Number of units	Number of units	Number of units	Number of units	Gross sales area	Net sales area
Hypermarkets	23	3	14	12	2	6	1	1	1	1	2	66	305,664	200,043
Supermarkets	129	-	47	27	2	18	15	3	6	-	1	248	269,010	174,362
Neighbourhood stores	333	-	52	43	18	3	46	3	66	-	1	565	200,552	116,053
Comfort stores	1	1	-	1	-	1	-	-	-	-	-	4	8,521	5,070
Convenience stores	1	-	-	-	-	-	-	-	-	-	-	1	159	83
Cash & Carry	13	-	5	-	16	-	-	-	1	-	-	35	115,946	79,610
Hard discount stores	7	-	-	-	-	-	-	-	-	-	-	7	4,671	3,401
Restaurants	22	7	-	-	-	2	-	-	1	-	-	32	9,869	5,954
TOTAL FMCG program	**529**	**11**	**118**	**83**	**38**	**30**	**62**	**7**	**75**	**1**	**4**	**958**	**914,392**	**584,576**
Home program	52	14	1	13	-	-	-	-	-	-	-	80	109,037	70,940
Furniture program	15	-	-	-	-	-	-	-	1	-	-	16	22,765	17,507
TOTAL home program	**67**	**14**	**1**	**13**	**0**	**0**	**0**	**0**	**1**	**0**	**0**	**96**	**131,802**	**88,447**
Clothing program and drugstores	**88**	**15**	**0**	**34**	**0**	**12**	**0**	**0**	**0**	**0**	**0**	**149**	**68,080**	**56,615**
Clothing program	71	8	-	34	-	8	-	-	-	-	-	121	64,890	53,887
Drugstores and perfumeries	17	7	-	-	-	4	-	-	-	-	-	28	3,190	2,728
Intersport	**31**	**10**	**0**	**27**	**-**	**9**	**-**	**2**	**-**	**2**	**-**	**81**	**51,134**	**39,122**
M holidays	**13**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**13**	**242**	**242**
TOTAL specialised programs	**132**	**25**	**0**	**61**	**0**	**21**	**0**	**2**	**0**	**2**	**0**	**243**	**119,456**	**95,979**
TOTAL retail units under management	**728**	**50**	**119**	**157**	**38**	**51**	**62**	**9**	**76**	**3**	**4**	**1,297**	**1,165,650**	**769,002**
Franchise stores	**224**	**-**	**30**	**49**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**303**	**55,219**	**36,611**
TOTAL	**952**	**50**	**149**	**206**	**38**	**51**	**62**	**9**	**76**	**3**	**4**	**1,600**	**1,220,869**	**805,613**

Comfort stores

Comfort stores are typically located in city centers. Their offer is adjusted to demands of the customers in a particular micro location (including highly demanding customers who expect in these stores excellent offer and services in some segments of the offer, e.g. select deli products, cheeses, wines, spirits, sweets etc.). With comfort stores Mercator is present in four different markets in larger cities: Ljubljana (basement level of the Maximarket department store), Zagreb (Importanne), Sarajevo (Alta), and from the last year onwards, also in Belgrade (Beograđanka).

Customer segments

Our customers are classified into five basic segments. These segments are the same in all markets of Mercator Group's operations. The customers of respective segments differ from each other in terms of lifestyle, rational behaviour and shopping behaviour (frequency of shopping, value and content of the average shopping basket, preferred store format etc.).

In 2012, we took a step forward in segmentation and knowledge of shopping behaviour and desires of our customers as we introduced the aforementioned three-dimensional approach. The segments were carefully studied and sales approaches and activities were adjusted accordingly. For example, customers of one segment may be highly loyal to traditional brands; in this case, branded products are included in the regular campaign flyers sent out to these customers; for customers preferring products with the lowest price, we expanded the assortment with such products. Our strategy and activities address all segments as they are all important to us. Priority of each segment is adjusted according to the season (e.g. start of a new school year, holidays, gardening) and according to the results and target market shares in the segments as they were laid down.

Category management

At Mercator, categories are managed within an eight-stage process that includes definition and analysis of each category. This is followed by the definition of its role and goals. The next step is to prepare the strategy and approaches for the entire marketing mix (products, prices, promotions, place) which are of key importance for successful and efficient management of each category. Then, key performance indicators are monitored each month as short-term and long-term measures are implemented to improve them.

Mercator is managing over 150 different product categories. Among them, four are always in the spotlight: bread and other baked goods, fresh meat, fresh fruit and vegetables, and dairy products. These are the categories that the customers spend the most money on per year; where brand loyalty is high; and where price elasticity of demand is very high.

Late in 2012, we introduced the three-dimensional approach to category management, which means that each category is managed from the aspect of different store formats and different customers segments in order to please every customer at every Mercator store. The following goals are pursued within each category:

- establish quality multi-level offer of branded and private label products;
- offer competitive prices of branded and private label products;
- provide attractive offer for our customers through sales promotion activities;
- efficiently manage the retail area at the level of each product; and
- providing appropriate sales service in our stores (at the point of sales).

Marketing

The four-pillar strategy is integrated into every field of Mercator's operations; this includes the company's marketing activities. In 2012, Mercator Group's operations were consistent with the policies laid down: focus on the consumer and core activity; project optimization; selection of the right, profitable projects; and searching for opportunities for growth and improvement of the market position.

Focus

In marketing, we introduced projects whose goals were geared towards improving consumer confidence and satisfaction and towards successful continuous adjustment to the changes in shopping behaviour. The highlight of the year 2012 was the **umbrella campaign called Steps** which was created for the first time in cooperation with the consumers who actually contributed their material through social networks; the best posts were included in the campaign's TV advertisement.

The offer of home made Slovenian produce and products is increasingly important. We are committed to preserving the environment, nurturing tradition, and allow smaller growers to offer their products in our stores via direct delivery. Our most important guiding principle, however, is to satisfy the needs and demand of our customers. Thus, we added tradition and integration into the regional environment to increasing demand of our customers for seasonal home made products by launching the project "Iz domačih krajev" (Locally produced / From our country). We also introduced stands in the fruit and vegetable department; furthermore, stands were introduced in the bread, fresh meat, and wine departments as well. For each category, we pursued the activity that motivated the consumers to take part, for example in announcing an open invitation for proposals of solutions for fruit and vegetable packaging made of environmentally-friendly raw materials; voting for the most popular types of bread that were subsequently introduced in particular Slovenian regions; and choice of the most popular Slovenian regional wine which is now available to our customers at a discount.

As we focused on our core activity – fast-moving consumer goods – we steered the short-term sales promotion activities according to the desires of our customers. We introduced the **Good Price project** which involves products by renowned brands at favourable prices. The project includes FMCG products that represent an important share among consumer products in the average shopping basket.

Focusing on the consumer, we carried on the communication of the key **advantages of the Pika card customer loyalty system**. Now, the customers can win and use their loyalty points for the entire offer; they are also offered special Pika discounts for select products; in addition, the card allows postponement of the payment and payment in up to 24 instalments at a zero interest rate. For the segment of customers keen on shopping in the web store, we also allow the functionality of online payment for alimentary products and technical consumer goods using the Pika card.

Optimization

After studying the portfolio of our private label products, we **revised many products** both in terms of content and their design. This improved the appeal and competitiveness of these products which are available exclusively in Mercator stores.

Shoppers today increasingly value convenience; therefore, they do more of their shopping in smaller stores like neighbourhood stores and supermarkets. Responding to this trend, Mercator launched in 2012 the process of **modernization of retail network** in Slovenia and in Croatia. We comprehensively refurbished a large number of supermarket format stores: we introduced new technologies, visual identity, and transparent tagging; we revised the offer and level of service (e.g. adding the service of baking pizzas, extending the fresh produce departments, extending the offer of ready-made products); and we improved energy economy. We also introduced the naming and designation of the supermarket stores; as a result, 62 units now have a new appearance. We also launched the activities of refurbishment of smaller neighbourhood stores and optimization of their assortment; over 80 units were successfully refurbished. After the refurbishment, the stores are even more neatly designed and clearly laid out, and they also appear more spacious. There is greater stress on the most commonly sold products and products included in special offers; these are featured at the fronts of the racks, in baskets, and on pallets.

Profitability

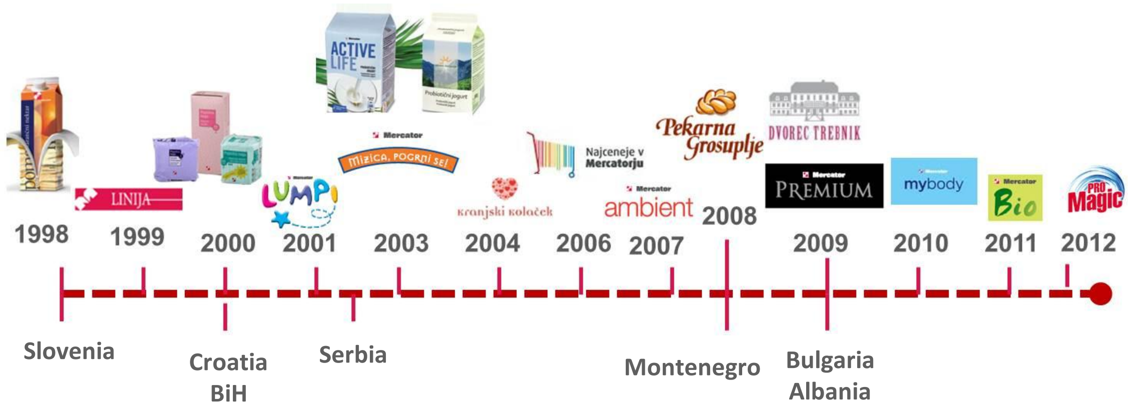
Private labels are an important tool of distinction and competitive advantage as the retailers use them to upgrade their offer, avoid direct comparison with the competition, improve the appeal of the offer, and to positively affect their own reputation to establish a long-term relationship with the consumers. The share of private label sales at European retailers has grown each year. Mercator was the first Slovenian retailer to offer its consumers **private label lines** which were gradually expanded to other markets of Mercator's operations. Introduction of private labels allows Mercator some control over the supply chain and targeted management in such way that allows offering the customers the best quality products at reasonable prices. The share of sale of private label products has been continuously rising. In 2012, Mercator Group saw a 14-percent increase in the share of private label in overall sales Group-wide.

The share of private label sales in total sales rose by 14 percent in all markets of Mercator's operations in 2012.

In 2012, we offered 2,783 private label products in our stores.

In addition to the private label products, consumers increasingly favour the low-priced products. In order to streamline their shopping experience and to promote the perception of Mercator as a retailer offering good prices, we reduced our regular non-alimentary offer in our larger store formats (hypermarkets and supermarkets) to allow more space for products included in special offers, and introduced a **new concept of labelling the special offer areas and seasonal departments**.

The picture below shows the development of private label lines and the year of the entry in foreign markets of Mercator's operations with the offer of private labels :



Current private label lines and their presence on Mercator's markets:

	SLOVENIA	CROATIA	SERBIA	BOSNIA AND HERZEGOVINA	MONTENEGRO	BULGARIA	ALBANIA
Mercator Naše ime, naš značaj.							
BONUS PLUS							
Mercator ACTIVE LIFE							
Mercator Minute							
LUMPI							
Pekarna Grosuplje							
Mercator mybody							
ambient							
Mercator PREMIUM							
Mercator comfort							
kranjski kolaček							
Mercator Bio							
TOTAL NUMBER OF PRIVATE LABEL LINES	12	11	10	7	5	4	7

Growth

Following the global trends of private labels, Mercator took a step further in developing **independent private labels** in select product categories, which can compete with renowned global brands. Independent labels have departed in terms of visual identity from the typical appearance of other private label products and there is no direct relation to the retailer's name. They involve the so-called "labels of new opportunities". Mercator's first independent private label of home cleaning and care products was named Pro Magic.

To date, Mercator retains the position of the only Slovenian traditional retailer that also offers FMCG through a web store. This channel has been further developed by **introducing the new Click&Collect service**. Following the model of international European retailers, our web store combines web ordering and collection of the order at the select store. The service is intended for highly mobile consumers who prefer web shopping and who find it more convenient to pick up their order on the way home from work or running errands, than waiting for the order to be delivered to their homes.

We have expanded the offer for our customers by introducing the new Click&Collect service.

In Slovenia, we launched the activity of awarding **discount on fuelling up at the Maxen petrol stations**. The coupon for discount on petrol is presented to Mercator customers in select market stores when the amount of their purchase exceeds a certain value. Providing a wide range of additional service, Mercator is offering its customers complementary services in a single place, at a single retailer. By offering related purchases (e.g. food and fuel), we reward the loyalty of our customers and offer the possibility of savings on household expenses.

Mercator will continue to grow through activities tailored to different customer segments (e.g. active families), product categories, or store formats. We shall emphasize the benefits for the consumers in each store format and adjust the sales promotion and other short-term activities accordingly.

REAL ESTATE MANAGEMENT AND RETAIL NETWORK DEVELOPMENT

In 2012, Mercator Group carried on the process of acquiring new sales area, especially by signing new lease contracts. We were also focused on refurbishments and updates of our existing retail network. The project Refreshment of FMCG Offer included refurbishment of 24 supermarkets in Slovenia and 8 supermarkets in Croatia, as well as a complete overhaul of Mercator center Belgrade ("Beograđanka").

***Beograđanka** is a prestigious store both in terms of offer (which includes, in addition to the basic offer, prestigious or gourmet products) and sales services (which present added value in shopping; the stress is on excellent service and fresh program), as well as overall appearance of the store (polished visual merchandising, attractive department layout, technological equipment).*

We opened the Mercator center Bršljin in Novo mesto, which includes a modern Mercator hypermarket; an Intersport, Modiana, and M Tehnika store; M holidays office; and over 30 outlets with supplementary offer for exciting shopping and relaxed socializing. The modern shopping center spanning a property unit of 38,103 square meters affords the customers a high level of shopping convenience and possibilities of socializing. The youngest visitors can enjoy the Lumpi children's playground spanning over 70 square meters. The customers may also use 391 parking spots, of which 91 are indoors.

In 2012, we also opened two Maxen petrol stations: one in Kranj and one in Ajdovščina.

Following are Mercator key goals in real estate management:

In 2012, we conducted various development activities to optimize Mercator's real estate management, and analyzed the possibilities of updating the concept of Mercator's shopping centers, improving the mix of products and services there, improving the mix of third-party providers, and establishing strategic partnerships with renowned international tenants.

As early as in 2011, the monetization project included an international tender to select an internationally renowned consultant, the global real estate consultancy Cushman & Wakefield from Great Britain; thus, the activities to carry out the project were commenced. Early in 2012, we defined a portfolio of real property intended for divestment – sale to international investors.

Monetization project has been temporarily put on hold; it will be resumed when the situation in the market improves.

In mid 2012, we obtained from the interested investors their non-binding offers for sale and leaseback of the selected part of real property portfolio in Slovenia. This was followed by development of documentation for the second round of negotiations with the selected investors. By obtaining the binding offers of short-listed investors, we completed the research stage in which we examined the possibilities of carrying out the monetization project. The answers we got were inconclusive and we decided that the project will be put on hold for the time being. Thus, Mercator has prepared the basis for instant resumption of the project in case the macroeconomic situation improves and ownership composition at Mercator is stabilized.

Investment and Divestment

In 2012, Mercator Group investment into property, plant, and equipment (CAPEX) amounted to EUR 67.3 million. 59.49 percent of this amount was used for investment in Slovenia, while 40.51 percent was used in foreign markets.

	Capital expenditure in 2012 (in EUR thousand)	Composition (in %)
Slovenia	40,054	59.49%
Serbia	19,085	28.35%
Croatia	3,589	5.33%
Bosnia and Herzegovina	3,396	5.04%
Montenegro	984	1.46%
Bulgaria	212	0.31%
Albania	10	0.02%
TOTAL	**67,330**	**100.00%**

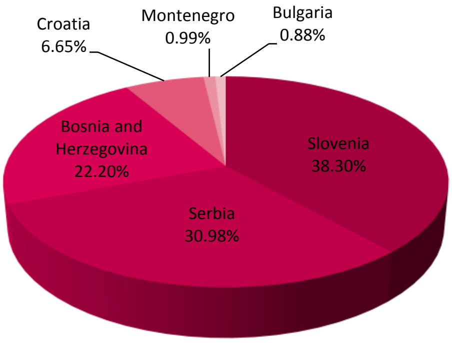
Investment into expansion of retail area represented 52.45 percent of total investment; refurbishments of existing units accounted for 32.95 percent; remaining 14.60 percent was invested in logistics, IT, and non-trade activities.

In 2012, the Group acquired 56,908 square meters of new gross retail area, of which 74% was obtained by operating lease and 26% by acquisitions and construction, or reconstruction of existing facilities.

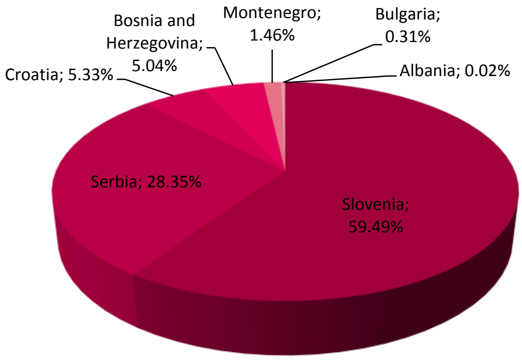
In 2012, Mercator Group divested EUR 6.8 million worth of property, plant and equipment.

In 2012, Mercator Group invested over EUR 67 million into property, plant, and equipment, while divestments amounted to EUR 6.8 million.

Share of newly launched facilities by markets:



Share of investments by markets:



Summary of total gross retail area as at December 31, 2012:

Gross retail area in m^2	Used for own operations	Leased out	Total as at Dec. 31, 2012
Owned retail area	798,018	193,979	991,997
Leased retail area	367,632	28,365	395,996
Total retail area	**1,165,650**	**222,344**	**1,387,993**
Owned warehouse capacity	137,141	575	137,716
Leased warehouse capacity	51,667	0	51,667
Total warehouse capacity	**188,808**	**575**	**189,383**
Owned commercial facilities	28,170	2,410	30,581
Leased commercial facilities	6,109	43	6,151
Total commercial facilities	**34,279**	**2,453**	**36,732**
GROSS AREA UNDER MANAGEMENT	**1,388,736**	**225,372**	**1,614,108**
- of which owned	963,329	196,964	1,160,293
- of which leased	425,407	28,408	453,815

SUMMARY OF RETAIL UNIT LAUNCHES BY MARKETS IN 2012

SLOVENIA
Area of new facilities: 21,796 m^2
Number of retail units: 9
Openings:
MC Novo mesto Bršljin, M Tehnika DOM in BTC in Ljubljana, hypermarket in shopping center Supernova in Nova Gorica, Modiana Outlet in Ljubljana (Šmartinska 102), Tehnika Outlet in Maribor (Tržaška 14), Department store Ljutomer, Furniture store Ptuj, superettes in Veržej and Križevci
Other openings: petrol stations in Kranj and Ajdovščina

CROATIA
Area of new facilities: 3,782 m^2
Number of retail units: 5
Openings:
Modiana in City Center One East in Zagreb, superette in Vodice, M Tehnika store in Umag, superette Kurilovec and superette Savica in Zagreb

SERBIA
Area of new facilities: 17,632 m^2
Number of retail units: 6
Openings:
Roda center Valjevo, Roda center Kruševac, supermarket in Čačak, hypermarket Beograđanka in Beograd, supermarket Mirijevo in Beograd, supermarket in Kikinda

BOSNIA AND HERZEGOVINA
Area of new facilities: 12,636 m^2
Number of retail units: 31
Openings:
Stores of the company Drvopromet (28 units) on total area of 10,991 m^2, supermarket in Laktaši and supermarkets Obilićevo and Nova Varoš in Banja Luka

MONTENEGRO
Area of new facilities: 561 m^2
Number of retail units: 2
Openings:
Superette Dobrota in Kotor, superette Lješnica in Bijelo polje

BULGARIA
Area of new facilities: 501 m^2
Number of retail units: 1
Openings:
Superette Dianabad in Sofia

EFFECT OF ECONOMIC CONDITIONS AND COMPETITION ON MERCATOR GROUP OPERATIONS IN 2012[1]

Economic conditions in 2012

Despite the feeble ray of optimism towards the end of 2011, 2012 proved the hardest year since the onset of the financial crisis. Despite the forecasts of GDP growth in all markets of Mercator's operations, growth rate actually dropped in the three key markets, i.e. Slovenia, Croatia, and Serbia; moreover, further decline in economic growth is anticipated at least for Slovenia in 2013 as well. Credit ratings of Slovenia and countries of Southeastern Europe continued to drop or, at best, remained at the same low levels. This in turn resulted in lower ratings of commercial banks and the related increase in financing costs.

Slovenia's economy has strong ties to the economy of the European Union where GDP shrunk according to the European Commission's autumn forecast by 0.3%, or by 0.4% in the euro zone. Growth is expected to resume in 2013 when GDP is forecast to increase by 0.4%, or 0.1% in the euro zone; however, differences between individual member states will remain significant. Countries that had lost a lot in terms of competitiveness have begun to bounce back. Such changes, paired with structural reforms, will pave the way for a stronger and more evenly distributed economic growth in 2014 when GDP growth is projected at 1.6% in the EU and 1.4% in the euro zone. According to estimates, inflation will drop to 2.0% in the European Union in 2013 and 1.8% in the euro zone.

In 2012, the European Central Bank only intervened once in the money market: in July, it lowered the interest rate for main refinancing operations from 1.0% to 0.75%. The drop in the interest rate resulted in a decrease of the value of interbank offered rates in the euro zone, which dropped to historical lows in 2012 after a period of growth in 2011 when the average 6 month EURIBOR stood at 1.638%.

In the course of 2012, the value of 6 month EURIBOR was in constant decline. In mid December, it reached a historical low at 0.316%.

As at December 31, 2012 the 6 month EURIBOR stood at 0.320% while the historical low was seen only a few days earlier, on December 14, 2012 at a rate of 0.316%. For comparison, before 2012, the lowest EURIBOR rate was recorded on March 31, 2010 at 0.944%. Average 6 month EURIBOR in 2012 stood at 0.828% (in 2011 it was 1.638%; in 2010 it was 1.084%). The difference between the highest and lowest 6 month EURIBOR thus amounts to 129 percentage points.

Economic conditions and competition in the markets of Mercator's operations

SLOVENIA

Macroeconomic conditions

According to forecasts by the IMAD (Institute of Macroeconomic Analysis and Development), GDP growth in 2012 is expected to be negative at -2.0% due to a slowdown in international demand and shrinking domestic consumption; in 2011, growth of 0.6% was measured. For 2013, the gross domestic product is again anticipated to fall, this time by 1.4%. The trend is expected to reverse in 2014 when economic growth will presumably return to 0.9%. According to the EBRD, gross domestic product dropped by 2.5% in 2012; this is expected to be followed by a 2.0% drop in 2013. According to the Statistical Office of the Republic of Slovenia, inflation rate in 2012 amounted to 2.7%, which is 0.7 percentage point more than in 2011. Assuming persistently weak economic activity and absence of major pricing shocks from the international environment, IMAD expects the inflation rate to be around 2.0% in the following two years. Rating of the Republic of Slovenia continued to drop in 2012, a rating dated from August 2012 was A, with

[1] Economic conditions are commented based on the following data sources: IMAD (Institute of Macroeconomic Analysis and Development); ECB (European Central Bank); S&P (Standard&Poor's ratings services) and statistical offices or bureaus of individual countries.

negative outlook, most recent rating reported at the beginning of 2013 is A-, with stable outlook. In August, we also saw the highest average spread on 10-year Slovenian bonds in 2012 (average spread in August was at 6.81% while the August average in the euro zone was at 4.03%); the high of August and early September even exceeded the psychological mark of 7.0%, only to start declining thereafter.

Effect of market situation on consumption

Consumer confidence in Slovenia plummeted in 2012. Effect of the crisis as perceived by individuals in their everyday life was stronger in 2012 than in the year before. In the Marketing Monitor research conducted by the Slovenian Marketing Association (DMS) in autumn 2011, 72% of respondents said they personally felt the effects of the economic crisis in their daily lives. In spring 2012, the figure rose to 77% and in autumn 2012 it reached 80%. From the aspect of shopping behaviour, the trend of rationalization in consumption has grown even stronger. Consumers tend to purchase more low-priced products and prefer private label offer; they shop for products included in special offers and promotion campaigns; they split their shopping between several retailers and do more shopping in discount stores.

Competition

Retail market is relatively stable and consolidated; the trend of increasing role of discount stores and drug stores persists. In addition to the traditional retailers, discount stores are further increasing the already high level of competitiveness. Due to increased consumer sensitivity to pricing, high pressure on prices is expected.

SERBIA

Macroeconomic conditions

According to the estimate by the Serbian statistical office, the gross domestic product in Serbia dropped by 1.9% in 2012 while in 2011, it grew by 1.6%. In 2013, gross domestic product growth is expected to recover as it is forecast at 1.5%. EBRD's estimate for gross domestic product growth in 2012 is negative at -0.7%; for 2013, they predict growth of 1.1%. There was a considerable surge in the inflation rate in 2012 as it reached 13.0% at the annual level (7.0% in 2011). For 2013, the Serbian National Bank anticipates an inflation rate of 5.5%. Average exchange rate of the Serbian dinar in 2012 stood at RSD 113.17 per 1 EUR, while the average rate in 2011 was RSD 101.95 per 1 EUR, which means it depreciated by 11.0%. As at December 31, 2011, the Serbian dinar exchange rate stood at RSD 104.64 per 1 EUR; in 2012, the exchange rate on the last day of the year was at RSD 113.72 per 1 EUR. According to the forecasts for 2013, the Serbian dinar is not expected to exceed RSD 125 per 1 EUR. Serbia's rating dropped in 2012 to BB-, with negative outlook.

Effect of market situation on consumption

In Serbia, the GfK household panel data shows that household consumption has increased slightly as a result of rising consumer prices while frequency and amount of purchases did not change.

Competition

In addition to regional traders (Mercator, Idea), in Serbia are also present international dealers Delhaize, Intermarche and Metro. Position in the market is maintained also by domestic traders Dis and Univerexport. The retail is relatively less consolidated (top 10 retailers present 40% of the market), traditional retail (small, independent retailers) still accounts for more than half of the market. Further consolidation of the market and enter of the discount retail chain Lidl is expected.

CROATIA

Macroeconomic conditions

According to the estimate of the Croatian National Bank (HNB), gross domestic product growth, after staying at zero in 2011, will turn negative in 2012 to reach -1.8%; in 2013, growth is expected to rebound to 0.3%. According to the EBRD, gross domestic product dropped by 1.9% in 2012. This is expected to be followed by a 1.2% growth in 2013. Inflation rate rose considerably again: after staying at 2.3% in 2011, it jumped to 3.5% in 2012. In 2013, it is expected to drop slightly to 3.2%. Average exchange rate for Croatian kuna in 2012 rose from HRK 7.43 per 1 EUR in 2011 to HRK 7.52 per 1 EUR in 2012. As at the 2012 year end, the closing rate was HRK 7.55 per 1 EUR. Croatia's rating in 2012 was downgraded to BB+, with stable outlook.

Effect of market situation on consumption

According to survey of consumer confidence conducted by the company Nielsen (3rd quarter 2012), consumer confidence rate in Croatia is among the lowest in Europe. Nearly all consumers believe the country is in recession and 86% of them believe that this will be the case in the following year as well (70% believe the situation will grow even worse). Consumers also respond to recession by shopping for lower-priced brands and private label products. According to the household panel data provided by the company GfK, household consumption dwindled, partly because of lower frequency of shopping sessions and especially because of lower amounts purchased.

Competition

In Croatia, the most retail chains are present throughout the whole region of Mercator's operation. In addition to domestic traders (Konzum, Plodine, Diona, Tommy, KTC and retail association NTL and Ultragros), European retailers with their retail chains are also present in Croatian market: Schwarz Group (Lidl and Kaufland), Rewe Group (Billa and Bipa), Interspar, dm - drogerie markt and Metro as wholesale trader. The first 10 retailers have 80% of the market share; in the coming years, further consolidation of the market with the possibility of entry of new (discount) retailers is expected.

BOSNIA AND HERZEGOVINA

Macroeconomic conditions

According to the estimate by the Central Bank of Bosnia and Herzegovina, gross domestic product grew by 0.6% in 2012 (1.6% in 2011). Growth is expected to continue in 2013 at a rate of 1.0%. According to the EBRD, gross domestic product grew by 0.1% in 2012; this is expected to be followed by a 0.4% growth in 2013. The exchange rate of the convertible mark is pegged to euro at the rate of KM 1.95583 per 1 EUR. In 2012, inflation is estimated to 1.8%. In 2013, it is anticipated to stay at roughly the same level (2.0%). Very high unemployed rate standing at 28% is a major problem in Bosnia and Herzegovina. In March 2012, the rating of Bosnia and Herzegovina stayed at B; however, the outlook was changed from negative to stable.

Effect of market situation on consumption

In Bosnia and Herzegovina, household consumption dropped as a result of lower purchasing amounts.

Competition

The market of Bosnia and Herzegovina is less consolidated. International retail chains (Delhaize, Intermarche), regional retailers (Mercator, Konzum and Tuš) and a number of smaller and larger (Bingo) local retailers are present. In the coming years further consolidation of the market primarily through organic growth and acquisitions of existing traders in the market is expected.

MONTENEGRO

Macroeconomic conditions

Gross domestic product growth in 2012 is estimated at 0.5%, which is a considerable slowdown relative to 2011 when GDP grew by 3.2%. Inflation rate in 2012 exceeded the forecasts from late in 2011 and is estimated to have reached 6.5% according to the Montenegrin central bank. In 2013, economic growth is expected at 1.0% while the inflation rate is anticipated at 2.4%. According to the EBRD, gross domestic product grew by 0.3% in 2012; growth in 2013 is expected at 0.8%. Montenegrin official currency is the euro. Montenegrin rating did not change in 2012 and it remains at BB-, with stable outlook.

Effect of market situation on consumption

In 2012, retail in non-specialized stores offering mostly alimentary products dropped in Montenegro.

Competition

In Montenegro, local retailers Voli, Albona and Laković have retained an important market share. Two of the major foreign retailers present in Montenegro are, Mercator and Delhaize. Take-over of the smaller retail chains, and thus greater market consolidation is expected in the future.

In 2012, international markets of Mercator's operations saw depreciation of the Serbian dinar and Croatian kuna, high level of unemployment and inflation in most markets, and strong competition.

PERFORMANCE ANALYSIS

Mercator Group performance in 2012

In 2012, situation in the markets was heavily affected by the economic crisis. There is still high uncertainty regarding economic recovery. Furthermore, financing sources are still very difficult to obtain. The slowdown of economic activity in Slovenia since the onset of the economic crisis has been greater than in European countries on average. In some markets of Mercator's operations, unemployment rate continues to rise and consumers act more rationally. All this had a negative impact on the trade activity.

In 2012, Mercator adopted several cost rationalization measures which resulted in savings of EUR 10 million in the second half of the year.

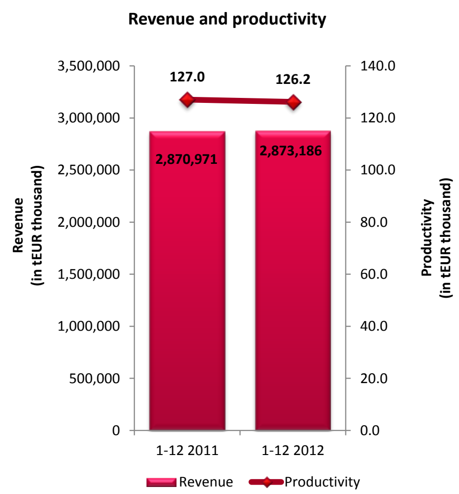
In Mercator, we regularly monitored the changes in the market and tried to curb all negative effects. We adopted several different measures to attain higher cost rationalization and to make our operations more efficient. Accordingly, we defined the fundamental strategic goals, i.e. optimization, profitability, focus, and growth which have been integrated in all fields of our operations. Furthermore, we focused more actively in 2012 on the optimization of working capital at all Mercator Group companies, which led to better liquidity of our assets.

Following is an analysis of performance for 2012, focused on the Mercator Group. The parent company Poslovni sistem Mercator, d.d., has a double role in the Mercator Group: it is the controlling company that holds ownership shares in the Group's subsidiaries; at the same time, it is an operating company carrying out all trade and other activities in Slovenia. Hence, it is sensible to focus for the purpose of performance analysis only on the consolidated financial statements that represent the performance of the Mercator Group as a uniform business entity. In addition, due to the transfer of a part of operating activities to the company M - Tehnika, d.d., in 2012, financial statements of the parent company Poslovni sistem Mercator, d.d., are not comparable in all categories between the periods.

Sales revenue and productivity

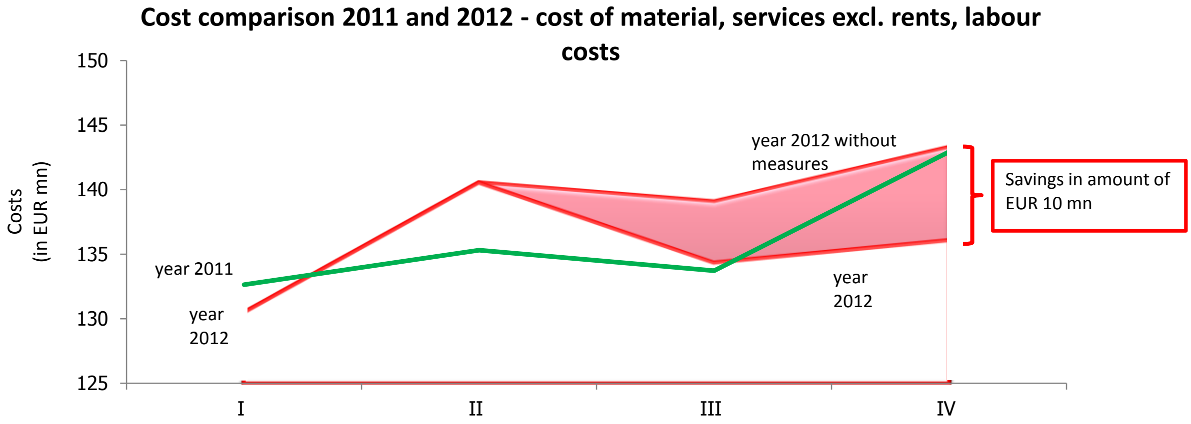
Revenue in 2012 remained approximately the same as in the year before, amounting to EUR 2,873 million. In Slovenian market, revenue dropped by 2.6%, particularly in the program of home products. The drop in revenue is above all a consequence of harsh economic conditions, stringent competition, and lower investment into retail network development; partly, the decrease of sales was also affected by the sale of the company Eta, d.d., in 2011. Revenue growth in international markets, reaching 3.7%, is above all a result of the takeover of the trade operations of the company Drvopromet in Bosnia and Herzegovina.

There was a slight decrease in productivity relative to 2011 – by 0.7%, which is consistent with the changes in revenue and number of employees.



Operating costs

Particularly in the second half of 2012, several measures were implemented to improve cost efficiency. By the end of the year, these measures brought savings of EUR 10 million. A high increase was seen in rent payments as Mercator is increasingly using operating lease to expand its retail network.



Cost of goods sold and selling costs of the Mercator Group, which include the cost of goods sold, production costs, selling and marketing expenses and other operating expenses in 2012 amounted to EUR 2,745 million and are 1.5% higher than in 2011.

Administrative expenses in 2012 amounted to EUR 130,416 thousand, and are 35% higher than in 2011. Administrative expenses also include the costs and expenses associated with the exit from the markets of Bulgaria and Albania.

Impairment of property and equipment and intangible assets present EUR 59,842 thousand.

Results from operating activities

In 2012, Mercator Group ran an operating loss of EUR 42.1 million. Negative results from operating activities are a consequence of non-recurring impairments and write-offs; in addition, harsh economic conditions and stringent competition in the market also contributed to poorer performance.

Net finance expenses

In 2012, net finance expenses amounted to EUR 68,132 thousand, which is 19.7% more than in the year before. Higher net finance expenses are to a great extent the result of negative currency translation differences due to depreciation of the Serbian dinar and Croatian kuna, in the amount of EUR 9,363 thousand, and higher impairment of receivables amounting to EUR 11,198 thousand. Despite the decrease in the EURIBOR, finance expenses for interest payments remain high due to high interest rate margins.

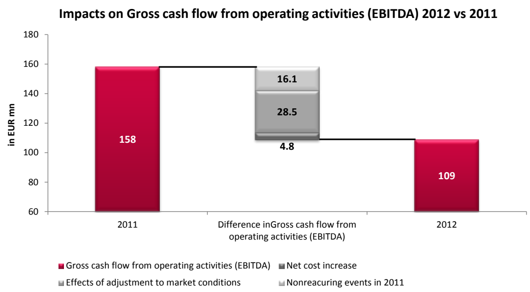
Profit for the year

Despite extensive cost rationalization measures, Mercator Group saw a net loss of EUR 104.6 million in 2012. Economic conditions in the market were still very challenging in 2012 and a major part of the loss is represented by impairments and write-offs, totalling at EUR 75,506 thousand.

In 2012, drop of results from operating activities was affected by impairment of real estate and intangible assets, as well as costs of exit from the markets of Albania and Bulgaria.

Effects on decrease of Gross cash flow from operating activities (EBITDA)

In addition to poorer performance of non-core activities Modiana and Tehnika, major reduction in the difference in price in the sale of FMCG also affected business performance of Mercator Group in 2012.

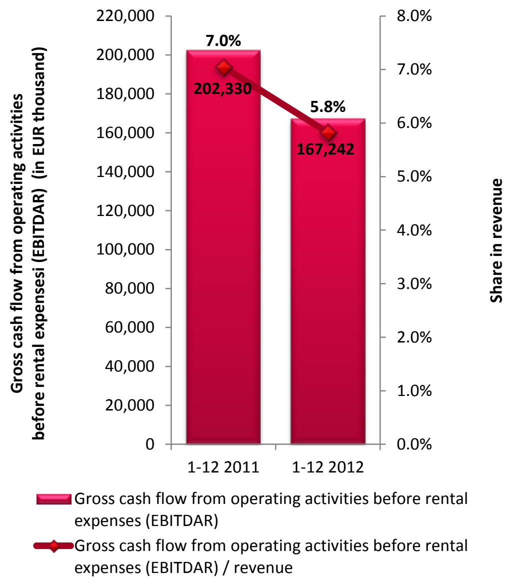


Gross cash flow from operating activities in 2011 also includes non-recurring items that positively affected this figure in the amount of EUR 16.1 million. Non-recurring effects include especially received payments for damages, including the damages for breach of competition clause in the Serbian market.

Gross cash flow from operating activities in 2012 was negatively affected by higher rental expenses which grew by EUR 14,315 thousand or 32.4%, mostly as a result of an increase in rented retail and warehouse area, as well as expenses related to refurbishment of retail network, expenses related to integration of retail units of Drvopromet, and expenses for modernization of IT.

Mercator Group Gross cash flow from operating activities in 2012 amounted to EUR 108.7 million which is 31.2% less than in the year before, for the same reasons that are listed with regard to lower results from operating activities. In comparison to the year before, Gross cash flow from operating activities before rental expenses is also lower, by 17.3%. The decrease is lower than the decrease in Gross cash flow from operating activities due to the increase in the amount of rental expenses for operating leases, which translated to an increase in rental expenses.

Gross cash flow from operating activities before rental expenses (EBITDAR) and share in revenue



Assets

Relative to the end of 2011, the value of Mercator Group assets as at December 31, 2012, was lower by EUR 90,839 thousand, mostly as a result of decrease of property, plant, and equipment, and inventories. Company assets as at December 31, 2012 amounted to EUR 2,522,820 thousand.

Mercator Group non-current assets as at December 31, 2012 amounted to EUR 1,967,797 thousand, which is EUR 58,758 thousand less than at the end of 2011. The greatest share of non-current assets is represented by property, plant, and equipment (96.4%), the value of which is EUR 49,014 thousand lower than in 2011 as a result of annual amortization and depreciation, lower investment, negative currency translation differences, and changes in the fair value of property, plant, and equipment based on the appraisal of real property as at October 31, 2012.

Mercator Group current assets as at December 31, 2012 amounted to EUR 555,023 thousand, which is EUR 32,081 thousand less than at the end of 2011. The largest share thereof includes inventories (48.2%) and trade and other receivables (43.2%). Decrease in the value of inventories is a result of efficient working capital management.

Activities to improve the working capital allowed us to cut the value of inventory by 14 percent in 2012 relative to the end of 2011, i.e. by more than EUR 42 million.

Equity and liabilities

As at December 31, 2012 company equity amounted to EUR 663,249 thousand. Key changes in equity in 2012 include the following: loss of EUR -104,555 thousand; currency translation reserve in the amount of EUR -18,544 thousand; and revaluation of property in the amount of EUR 55,137 thousand.

Mercator Group's borrowings and other financial liabilities as at December 31, 2012 amounted to EUR 1,094,720 thousand, which is EUR 90,013 thousand less than at the end of 2011. Decrease in borrowings and other financial liabilities is a result of efficient activities to reduce the Group's debt. Net financial debt of the Mercator Group as at December 31, 2012 amounts to EUR 1,008,034 thousand, which is 7.6 percent lower than the 2011 figure.

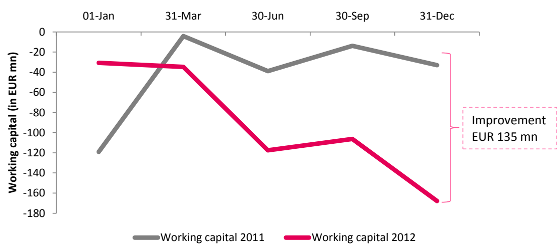
Trade and other payables as at December 31, 2012 amounted to EUR 675,320 thousand, which is EUR 88,969 thousand more than at the end of 2011. Increase in trade and other payables is related to deleveraging and optimization of working capital.

Provisions as at December 31, 2012 amounted to EUR 31,459 thousand, which is EUR 1,252 thousand less than as at the end of 2011, especially due to partial reversal of provisions for restitution claims, severance packages, and rewards for loyal service.

As at December 31, 2012, long-term coverage of non-current assets with non-current liabilities at the Mercator Group amounted to 68.3%, which is 13.7 percentage points less than as at the end of 2011.

Changes in working capital

Improvement of working capital management is all the more important in times when economic conditions are harsh. In 2012, Mercator Group succeeded in releasing additional financial assets tied up in working capital. Compared to the end of 2011, net working capital was cut by EUR 135 million.



Review of write-offs, revaluation adjustments, and impairments

A major factor of negative results from operating activities were write-offs, revaluation adjustments, and impairments, which amounted to a combined total of EUR 75.5 million.

Impairment of real estate

Pursuant to the corporate accounting policies, Mercator Group re-appraised its real property to fair value in 2012. Real estate impairment had a negative effect of EUR 35,118 thousand on the income statement; however, the overall effect of real estate appraisal was positive as it increased the equity by EUR 20,402 thousand as a result of value increases recognized in revaluation adjustment to equity.

Impairment of intangible assets

Goodwill impairment amounted to a total of EUR 5,885 thousand, with impairments pertaining to the following:

- Takeover of the company Presoflex, d.o.o., Croatia, in the amount of EUR 4,360 thousand, which was entirely impaired in 2012.
- Goodwill generated in the 2005 takeover of the companies Era Tornado, d.o.o., and Trgohit, d.o.o., in Croatia in the amount of EUR 1,579 thousand, was impaired by EUR 688 thousand in 2012.
- Remaining goodwill in the amount of EUR 837 thousand was entirely impaired in 2012.

Impairment of other intangible assets in the amount of EUR 6,977 thousand pertains to impairment of the Getro brand and other minor impairments to intangible assets.

Costs of withdrawal from the markets of Albania and Bulgaria

Pursuant to the adapted strategy of exit from the markets of Albania and Bulgaria, Mercator Group recognized in 2012 in the income statement expenses related to the exit from these two markets, amounting to EUR 17,470 thousand. Costs and expenses relate to liquidated damages for termination of lease contracts in Bulgaria and Albania; impairment of investments into foreign fixed assets; revaluation adjustment equipment and inventories; and recognition of provisions for employee's severance packages.

Other non-recurring items

In 2012, Mercator Group also recognized revaluation adjustments to receivables, in the amount of EUR 11,198 thousand, which is EUR 5,897 thousand more than the figure for 2011. The increase is related to recognition of revaluation adjustment to trade receivables, revaluation adjustment for rental expenses paid in advance in Serbia, and revaluation adjustment to receivables regarding accounting of charges on offset payment for meal allowance and holiday/annual leave allowance.

PERFORMANCE ANALYSIS BY MARKETS

Slovenia

In Slovenia, market conditions involved a slum in the gross domestic product and a higher inflation rate. Both confidence and purchasing power of consumers are low; shopping is rational and expectations for the future are pessimistic. In 2012, the company Mercator, d.d., increased its ownership share in the company Vesna, Trgovsko podjetje, d.d., from 45% to 100%. Thus, it acquired seven retail units which were previously in operation as franchise stores. Results in Slovenia are somewhat poorer than in the year before. Revenue amounted to EUR 1,618.5 million in 2012, which is 2.6% less than in 2011. Lower revenue is mostly a result of adjustment of the customers to the harsh economic conditions as they reduced the frequency of shopping sessions and value of the average shooping basket. Moreover, revenue from sales of home products dropped again as a result of a decrease in sales of more durable goods, and closing down of some stores. In 2012, cost optimization and operations rationalization measures were intensively implemented in the field of working capital management, cost rationalization, and improvement in productivity of employees. Moreover, marketing activities were carried out with the purpose of increasing customer satisfaction.

Serbia

In Serbia, too, economic conditions were negative as the gross domestic product shrunk and inflation rate was high. Serbian consumers responded to the economic conditions and lower purchasing power by changing their shopping behaviour, focusing on simple shopping and looking for the most inexpensive product. Depreciation of the Serbian dinar had a major impact on the performance in Serbia. Relative to December 31, 2011, dinar depreciated by 8.7%. Revenue amounted to EUR 560.9 million in 2012, which is 1.4% more than in 2011. The growth was a result of opening of 6 new units with a total area of 17,632 square meters and several franchise units. Cost rationalization measures had a positive impact as it led to lower costs, excluding rental expenses.

In 2012 in Serbia a Decree on restriction of margins on basic foods was in force. Thus increased VAT rate in the last quarter of the year had a negative impact on gross margin.

Croatia

In Croatia, Mercator's performance was worse than in 2011, which is mostly the result of weak macroeconomic situation, low consumer purchasing power, growing competition, and increase in the VAT rate. Revenue in Croatia amounted to EUR 381.4 million, which is 7.3% less than in 2011. We saw a minor slip in sales under the Mercator brand, and a somewhat more significant decline in the sales under the Getro brand. Lower sales in 2012 were a result of high fixed costs and several openings of competitors' retail units in direct vicinity of Mercator and Getro stores. Cost control measures notably reduced the operating costs at the company.

Responding to poor performance and loss, a program of restructuring and revival of the company was adopted. In order to reap the synergies to be brought about by Croatia's anticipated accession to the EU on July 1, 2013 the Group Management Board merged the operations of Mercator, d.d., and Mercator - H, d.o.o., under single management. The goal of the project is to attain a higher level of connection between all business functions and to define the ways in which business synergies are to be reaped between the two countries. Croatia's accession to the EU will release the cross-border flow of goods and services, which will make operations much easier and which will allow us to use single logistics infrastructure for both countries, to optimize the use of logistics capacities and other infrastructure, and to optimize our suppliers. Merging of business functions also includes cutting operating costs and unifying the development of joint solutions through consideration of local use. Furthermore, joint management is sensible because of the similarities in terms of consolidation of the two markets and because the expectations and requirements of Croatian customers are similar to those of the Slovenian customers.

Activities to establish central management of operations for the markets of Slovenia and Croatia after the latter's accession to the EU are in progress. These activities are expected to result in savings as business synergies between the two countries are reaped.

Bosnia and Herzegovina

Rising inflation rate, slower growth of gross domestic product than in the year before, and exceptionally high unemployment rate bore a negative impact on the purchasing power of the population. Nevertheless, we succeeded in increasing our sales in Bosnia and Herzegovina relative to 2011. Revenue in Bosnia and Herzegovina amounted to EUR 194.1 million in 2012, which is 48.7% more than in 2011. Revenue growth was positively affected by the acquisition of retail units DP Marketi of the company Drvopromet, d.o.o.; expansion of wholesale activities; and successful response to the changes in consumer behaviour.

Montenegro

Macroeconomic conditions in Montenegro saw further aggravation in 2012. Gross domestic product growth was slower than in 2011 and inflation rate remained high. Despite lower purchasing power and mounting pressure on the prices exerted by competing retailers, revenue in

Montenegro in 2012 rose by 4.1% to EUR 104.8 million. Solid performance is also a result of timely response to the changes in consumer behaviour, and effective implementation of cost rationalization measures. Revenue increased especially in wholesale and as a result of newly opened and refurbished units. Correct and timely implementation of cost control measures resulted in lower costs of material and services excluding rental expenses, and labour costs; in addition, the share of these costs in revenue was lower than in the year before.

Bulgaria and Albania

Estimated GDP growth in the Bulgarian market in 2012 is 1.0% and inflation rate is estimated at 3.0%. Bulgarian rating is BBB, with stable outlook. For Albania, economic growth estimate for 2012 is also low at 0.5% while inflation is estimated at 2.0%. Albania's rating is B+, with stable outlook. Both markets saw relatively high unemployment rate which means lower purchasing power of the consumers.

Performance in both Bulgaria and Albania was sub-par. In Albanian market, sales revenue was lower than in the year before, also as a result of a cut in advertising activities and the fact that our competitors stepped up their efforts. Pursuant to the adopted strategy, we exited the Albanian market at the end of 2012, while exit from Bulgaria is planned for 2013.

(in EUR thousand)	Slovenia	Serbia	Croatia	Bosnia and Herzegovina	Montenegro	Bulgaria	Albania	Mercator Group
Net revenue	1,618,467	560,887	381,429	194,053	104,786	9,269	4,295	**2,873,186**
Share Group net revenue	56.3%	19.5%	13.3%	6.8%	3.7%	0.3%	0.1%	**100.0%**
Gross cash flow from operating activities (EBITDA)	82,685	26,912	-2,297	5,904	1,633	-4,793	-1,299	**108,745**
Gross cash flows from operating activities (EBITDA) / net revenue	5.1%	4.8%	-0.6%	3.0%	1.6%	-51.7%	-30.2%	**3.8%**
Gross cash flow from operating activities before rental expenses (EBITDAR)	88,975	43,101	16,897	14,727	7,279	-3,216	-521	**167,242**
Gross cash flows from operating activities before rental expenses (EBITDAR) / net revenue	5.5%	7.7%	4.4%	7.6%	6.9%	-34.7%	-12.1%	**5.8%**

Mercator Group performance plans for 2013

For 2013, macroeconomic analyses forecast further aggravation of economic conditions and persistent stagnation of economic activity. Instability in financial markets and expansion and deepening of the debt crisis affect the banks' lending terms which are not expected to improve in the next year. Economic conditions have lead to major changes in consumer behaviour. The shopping basket has become smaller and more modest; it includes more inexpensive products and a higher share of private label items.

Mercator Group performance plans for 2013 are based on the Group's starting points specified in the Medium-term business plan for the period 2013–2016. Additionally, the plans include the current changes and developments in the region's economies and specific events that are expected to bear a notable effect on the Group's performance in the period ahead, including:

Monetization project has been temporarily put on hold

Because of inadequate offers, the monetization project was temporarily put on hold. Resumption, or revival of the project is possible and we shall proceed with it when circumstances related to the macroeconomic environment are normalized, when ownership structure is stabilized, and when debt markets are normalized and stabilized.

Group reorganization

The process of reorganization of the Mercator Group will have a notable effect on the increase of efficiency, and rationalization of labour costs and processes.

Withdrawal from Bulgaria and Albania

Due to unprofitable operation of the companies and focus on improvement of performance in the key markets, Mercator launched late in 2012 the activities to exit the Albanian market. Hence, business units in this country ceased to operate as of December 31, 2012. In 2013, the Mercator is planning to withdraw from Bulgaria as well.

Focus on the core activity

Pursuant to our strategy, we are focusing on performance improvement in the core activity, i.e. FMCG program. In times of harsh economic conditions, home product and other business activities like the textile product tend to be severely hit. In order to improve its operations, Mercator launched the key strategic projects of restructuring and revival of these companies, which includes rationalization of cost efficiency through merging of the companies with Mercator companies in particular markets.

Reaping synergies at the Group level

Establishment of global supply and consolidation of suppliers are planned for all markets of our operations. Activities are planned to improve category management and to optimize the assortment.

Strategic projects in 2013

Optimization of retail unit operations and improvement of competitiveness

We shall restructure our sales network in order to optimize operations and enhance the level of service at the stores. We shall focus on smaller store formats like supermarkets and neighbourhood stores that offer consumers everyday solutions at every step. Major emphasis is placed on product assortment as we look to offer quality products at reasonable prices, as well as on private label development.

Cooperation with the suppliers in order to improve the value added

Establishing global supply is an important process as it will allow us to focus on the purchasing and sourcing strategies of individual categories and to reap market synergies. Croatia's entry into the European Union will open up the possibilities of greater synergies in supply of trade goods; subsequently, other markets of operations are planned to be included as well. According to the needs of the consumers, we shall restructure the offer of individual store formats in order to boost the volume of sales and to allow easier planning of production output for our suppliers, thus generating savings in the supply chain.

Cost control measures are focused on reorganization of business processes

The measures adopted to rationalize operations involve focus on lowering the operating costs, stopping non-essential investment projects, optimizing logistics costs, and more rational use of energy. Furthermore, reorganization of operations is planned. It is focused on revision of key and support processes at Mercator Group companies, which will lead to higher productivity and optimization of administrative work.

Revision of the Pika card customer loyalty system
As of February 1, 2013, we introduced a new Pika card customer loyalty system. Now, consumers receive one point per each euro paid. Another novelty is that points are awarded when customers pay with cash, as well as when they use other debit or credit cards. Moreover, the offer of products included in special offers for Pika card holders will be extended; thus, they will benefit from their discounts immediately.

Key projected economic indicators for year 2013

	1-12 2012	Plan 2013	Indeks Plan 2013/ 1-12 2012
Revenue (EUR thousand)	2,873,186	2,900,526	101.0
Results from operating activities (EUR thousand)	-42,147	64,747	-
Profit before income tax (EUR thousand)	-110,279	6,070	-
Profit for the financial year (EUR thousand)	-104,620	3,025	-
Gross cash flow from operating activities (EBITDA) (EUR thousand)	108,745	142,368	130.9
Gross cash flow from operating activities before rental expenses (EBITDAR) (EUR thousand)	167,242	199,888	119.5
Capital expenditure (EUR thousand)	67,330	50,000	74.3
Return on equity	-13.7%	0.4%	-
Return on sales	-3.6%	0.1%	-
Gross cash flow from operating activities (EBITDA) / revenue	3.8%	4.9%	129.7
Gross cash flow from operating activities before rental expenses (EBITDAR) / revenue	5.8%	6.9%	118.4
Net financial debt / equity	1.52	1.28	84.0
Number of employees based on hours worked	22,769	22,797	100.1
Number of employees as at the end of the year	23,920	23,417	97.9

RISK MANAGEMENT

Expectations that 2012 would be an economically harsh year were correct. In the region of Mercator Group operations, economic activity slowed down and the rate of unemployment rose in most markets, which – combined with increase in consumer prices and low growth of average wage – resulted in further slump of consumer purchasing power. This was reflected in notable drop in retail demand, as well as in the persistence of the trend of uncertainty with regard to financial risks which were not common in the period before the crisis. In such harsh and uncertain environment, it was crucial for Mercator Group to carefully manage the risks that it faces in its business operations.

Managing the key risks in 2012

At the Mercator Group, we are constantly re-examining and analyzing the existing and potential new risks, as we devise and implement the measures for their management. 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 which were therefore most closely monitored and controlled in 2012.

Overview of key risks by areas:

RISKS	Assessment of the change in exposure 2013/2012
Business Risks	
• Risk of a decline in purchasing power	
• Risks of suboptimum marketing mix and effects of the competitive environment	
• Risks of failurte to attain the planned profit margin	
• Risks in the supply process	
Financial Risks	
• Credit risk in wholesale	
• Pika card credit risk	
• Currency risk	
• Interest rate risk	
• Liquidity risk	
Operational Risks	
• Category management operational risks	
• Core activity operational risks	
• IT risks	
• Environmental risks	
• Human resource risks	

Legend:
- Risk will decrease
- Risk will remain the same
- Risk will increase

Business Risks

Business risks are related to company operations and our core activity.

Key risk	Risk management analysis for 2012	Planned activities	Assessment of the change in exposure 2013/2012
Risk of a decline in purchasing power *Assessment of the risk of a decline in purchasing power (size of market) due to challenging economic conditions*	The unemployment rate is the key indicator of purchasing power and the sense of security on the part of the consumers. In the last year, this category has reached the highest levels in the last five years in the key markets of Mercator's operations. Furthermore, there has been a drop in GDP while consumer prices rose at a higher rate than wages. Mercator does not have direct control over the risk of a decline in purchasing power. We adapt to the market conditions with suitably pricing policy and other activities aimed at providing the right offer for our consumers and keeping the revenue at the attained levels. Regular monitoring of key macroeconomic indicators (unemployment, GDP, inflation, etc.) and their effect on the operations of the company and the trade industry in all markets is a precondition for adopting the right business decisions.	We have adapted the marketing activities to the new conditions in order to provide adjusted offer for our customers, and to retain our revenue level. Adjustment of operations to the harsh market conditions involves the following measures: • investment into prices, • comprehensive revision of the customer loyalty system and adjustment of promotional activities.	
Risks of sub-optimum marketing mix and effects of the competitive environment *Assessment of risk based on market conditions and Mercator's position in the markets of operations*	Risks of sub-optimum marketing mix and effects of the competitive environment represent a group of risks based on the generally accepted definition of the marketing mix which includes price, place, promotion, and product. Highly competitive environment in all markets in 2012 compelled us to monitor our competitors even more closely with regard to every aspect of the marketing mix, and to respond promptly with the marketing mix management tactics. In Slovenia, we saw minor relative improvement of the market position, which was a result of more efficient marketing mix management.	Further improvement in the efficiency of marketing mix management with simplified strategies and tactics for each category (particularly for target categories), based on shopping behaviour of consumers and measures implemented by competitors, from the following aspects: • pricing management based on regular monitoring of competitiveness of our regular retail prices, • successful, efficient, and simple promotional activities for key products, • active assortment management for both branded and private label products, • consistent management of sales area including planograms for the smallest stores. Monitoring the perception of the key elements of the marketing mix.	
Risks of failure to attain the planned profit margin *Assessment of the effect of further aggravation of economic conditions on the purchasing power and consequently*	Planned and actual key performance indicators for the entire FMCG format and for particular categories are regularly monitored at the company. In case of any undesirable deviation, short-term and long-term measures for the improvement of key performance indicators within each category or at the level of a particular product are implemented immediately. Profit margin is also among the key performance indicators. It is particularly	Due to the increasingly harsh economic situation and impaired competitiveness, additional investments in terms of pricing will be required; this will affect the profit margin attained. Another result of the expected drop in purchasing power will be the reduction of sales volume, which will also affect the profit margin.	

on the attained profit margin	closely monitored and decisions for improvement are adopted on a daily basis. Efficient and successful management of regular and promotional retail prices is of key importance.		
Risks in the supply process *Assessment of global and local impacts on Mercator's supply processes*	Local risks in the process of purchasing products for resale are rooted in the harsh economic conditions faced by our suppliers. Some of our suppliers have seen insolvency and bankruptcy proceedings instituted. The results are delivery failures and delivery of goods of inadequate quality. Global risks include risks of fluctuation of prices of tradable commodities (energy, basic foodstuffs) and exchange rate fluctuations which affect the purchasing prices of products at the Mercator Group. Local impacts are managed through transparent and clear operations with proven suppliers, which allows us to perceive any problems resulting from the economic hardship in a timely manner, and to adjust instantly to reduce the possibility of delivery failures. Regular monitoring and checking of supplier solvency, and annual assessment of suppliers allow timely redirection to new supply sources. Lower purchasing prices and better supply channels are attained by combining our procurement operations with those of the company Mercator-H, d.o.o., and our subsidiaries in Southeastern Europe.	Transparent relations with proven suppliers, instant response and timely redirection to new supply sources, regular monitoring and checking of solvency of our suppliers, and annual supplier assessment. Centralization of global supply in order to improve the procurement terms and conditions and to reduce the effect of input raw material price volatility on the production of products in target categories. We seek to mitigate local effects on the supply processes by managing the risks of delivery failures. Supply processes are supervised on monthly basis and corrective measures are adopted to reduce local risks in the supply process.	

Legend:

- Risk will decrease
- Risk will remain the same
- Risk will increase

Financial risks

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.

<table>
<tr><th>Key risk</th><th>Risk management analysis for 2012</th><th>Planned activities</th><th>Assessment of the change in exposure 2013/2012</th></tr>
<tr><td>Credit risk in wholesale

Assessment of the risk that receivables from business partners resulting from deferred payment will only be settled partly or not at all</td><td>We are monitoring daily the level and changes in the level of receivables to wholesale customers. Weekly reports on amount of receivables, with emphasis on receivables overdue by over 60 days

In 2012, general liquidity grew even worse than it was before, to which we responded by making our credit limit policy and receivables collection regime even stricter.

In 2012, revaluation adjustments and receivables write-offs amounted to EUR 11.2 million
<table><tr><th>EUR thousand</th><th>2011</th><th>2012</th><th>Index 2012/ 2011</th></tr><tr><td>Adjustment/ revaluation of receivables</td><td>5,301</td><td>11,198</td><td>211.24%</td></tr></table></td><td>Improvement in internal processes that allow better monitoring of receivables (fewer late payments in transfers of invoices).

Stricter terms of sale to customers exceeding the defined credit limits and to customers whose payments are overdue.

Additional stress on lowering overdue unpaid liabilities to Mercator

Increased bilateral or multilateral netting (netting by novation)

Hiring a third-party agency for the collection of overdue receivables

Monitoring exposure to individual customers at the Mercator Group level</td><td></td></tr>
<tr><td>Pika card credit risk

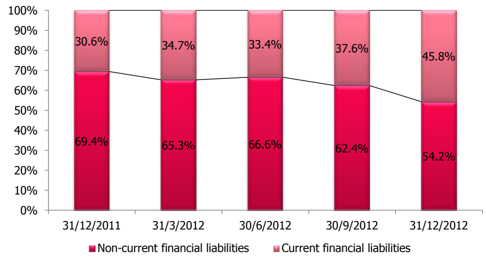
Assessment of the Pika card credit risks (possibility that receivables from customers, resulting from deferred payment, shall only be settled partly or not at all)</td><td>We are monitoring on a daily basis the changes in receivables from Pika card holders. In 2012, we continued strict implementation of measures to control these risks, and carried on the trend of lowering the percentage of unpaid receivables overdue by more than 60 days.</td><td>More active approach to management of defaults, including telephone notices as early as with the third written notice.</td><td></td></tr>
<tr><td>Currency risk

Assessment of the loss of economic benefit due to changes in exchange rate</td><td>Mercator Group is exposed to currency risk especially in the markets of Serbia and Croatia, in the segment of servicing financial liabilities of subsidiaries Mercator-H, d.o.o., and Mercator-S, d.o.o., resulting from international and local euro-denominated borrowings.

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.</td><td>Constant monitoring of macroeconomic background of the changes in the exchange rate at hand, and other related macroeconomic indicators and trends

In case of increase in the currency risk, the Group will decide on any additional measures for protection and hedging of this risk.

We shall implement a project HoldCo, through which we will reduce the dependence from unexpected exchange rate movements as a result of credit in local currencies (HRK and RSD).</td><td></td></tr>
</table>

Interest rate risk *EURIBOR interest rate is subject to market fluctuations and it is changing on a daily basis, which can lead to increased financing costs*	Mercator Group liabilities include some liabilities that are dependent on the changes in the EURIBOR variable interest rate. In 2012, the 6 month EURIBOR dropped from 1.606% to 0.320%, or by 80.1 percentage points. Average 6 month EURIBOR in 2012 was 0.828 %. The company holds derivative financial instruments for the purpose of hedging from the increase in reference interest rates: interest rate cap and interest swap.	Regular monitoring of the changes in variable interest rates and, given any forecasts of rising interest rates, examining the possibilities offered by derivative financial instruments in order to hedge the interest rate risk. At any moment, at least 50 % of all financial liabilities and at least 25% of total financial liabilities are hedged.	
Liquidity risk *Assessment of the risk that at a certain moment, the company will not have enough liquid assets to settle its current liabilities*	In 2012, we diversified our financial sources with 4 issues of 6-month commercial papers, amounting from EUR 5 to 12 million. Due to uncertainty in the financial sector, access to long-term sources is highly restricted. Furthermore, as the short-term parts of long-terms loans become due in 2013, the ratio between long-term and short-term financial liabilities declined. As at December 31, 2012, this ratio was 54.2% : 45.8% (69.4% : 30.6% as at December 31, 2011). Changes in composition by maturity for Mercator Group liabilities 2012:  	Multilateral agreements with banks regarding further financing. Notable improvement in working capital, searching for internal untapped potential, and diversification of financing sources. Liquidity management at the Mercator Group level according to the needs of each company.	

Legend:

- Risk will decrease
- Risk will remain the same
- Risk will increase

Operational risks

Operational risks are related to the progress of business processes and activities at the Mercator Group, and to the consumption and costs incurred in the progress of business processes.

Key risk	Risk management analysis for 2012	Planned activities	Assessment of the change in exposure 2013/2012
Category management operational risks *Increase of tradable commodity prices*	Circumstances in the raw material market are a result of concentration of ownership in particular industries, impact of weather, shrinking of arable land, as well as commodity market speculation. The company is constantly keeping track of the commodity market prices for those products that depend notably on such prices, and we adopt in a timely manner the measures that eliminate the negative effects. Since commodity market changes affect the prices of all products in a category, loss of sales and profit margin cannot be recovered by the use of substitutes.	Monitoring the commodity market prices for those products that depend considerably on the changes in raw material prices. Announcing tenders for production of private label products at a time when the prices of tradable commodities are lower. We are actively monitoring the changes in energy prices and their impact on manufacturer prices.	
Seasonal effect	Seasonal effect represents the risk the value of which involves estimating the possibility of AGM failure due to urgent decrease in profit margin for more efficient sale of seasonal gods We also look to reach agreements with the suppliers for additional discounts in case of additional price cuts or in case of return of goods following the end of season.	Monitoring of the inventory of seasonal products and adopting measures to clear such inventory. Reaching agreements with the suppliers for additional discounts in case of additional price cuts or in case of return of goods following the end of season.	
Core activity operational risks *Failure of the refrigeration system and electrical wiring*	At the Zalog and Bohova warehouses where there is a critical risk of refrigeration system and electrical wiring failure, the risk was successfully managed. The following measures were implemented: • training was held for refrigeration system operators, • protection equipment was maintained and inspected as scheduled; ammonia detection devices were regularly calibrated; breathing devices were inspected and tested; masks were cleaned, and air bottles/cylinders were inspected, • electrical installation was regularly maintained and switching blocks were cleaned, • ammonia indicators were installed in working areas with delayed detection, • measurements on electrical installations were conducted, • smoke sensors were fitted into switch blocks.	The following measures were implemented at the Zalog and Bohova warehouses: • restoration of electrical installations pursuant to the report on inadequate results of electrical measurements and tests, • repeated measurements of electrical installations after the restoration.	

IT risks	IT risks appear at the Mercator Group in management of business data, business IT systems, and internal business processes. We maintained an up-to-date backup copy of the key IT systems and we segmented and mirrored the key system elements.	We conducted current operating activities (monitoring of system operation and backup copying), implemented the IT Service Management principles, and modernized and optimized our IT systems.	
Environmental risks *Electrical energy*	We successfully managed the environmental risks. In order to cut power consumption, we developed a monthly environmental report for the users, which includes data on the quantity and value of power consumption. The users are provided quarterly notes on compliance with the measures for efficient use of energy. Pilot projects of establishing control over operation of refrigeration equipment are in progress at four selected units. The projects involve providing constant access to data on power consumption for refrigeration equipment, monitoring of this data, and compiling reports that make it easier to identify the problematic users of electricity (chests, cabinets, counters, chambers etc.) and to develop the measures required to cut power consumption. An agreement was signed with the company Petrol, d.d., on contractual co-financing of the replacement of the existing fluorescent lighting with LED luminaires in for garages and in the corporate visual identity light boxes and signs; grants will be obtained for these investments. Regarding planning and use of alternative sources of energy, a combined heat and power (co-generation) equipment was installed at nine trade facilities; additionally, an agreement was signed to install this technology at 37 new facilities.	At Mercator, d.d., we shall encourage all employees to comply with the Manual on efficient use of energy. We shall install additional combined heat and power equipment and update the boiler rooms. We shall replace the existing lighting with LED luminaires at garages and in lightboxes at select trade centers. At the company M-Tehnika, d.d., we shall provide comparison to the year 2012 for items that are monitored in the environmental reports. We shall also ensure correct accounting of data on volumes. At Mercator-H, d.o.o., we shall carry on the activities of the project of implementing the systems for control and energy efficiency. Also planned is the change of electricity suppliers and transition to those suppliers offering the best price for each rate. At Mercator-S, d.o.o., we shall amend the instructions for efficient use of energy and use these instructions as the basis for employee training. At Mercator-BH, d.o.o., we shall prepare and put into use the Rules and Regulations on Efficient Use of Energy.	
Human resource risks *The lack of deficit personnel*	For several years we monitor the deficit of operational personnel in deficit professions butcher, baker, ccok and waiter. To reduce the risk, we conducted regular activities for employment, including employment of foreigners, the use of variable pay and participation in the introduction of retraining in the deficit professions for those employees who have a successful track record.	We expect that the lack of deficit personnel will continue in 2013. To reduce the risk exposure we have agreed with external institutions (Employment Service of Slovenia) on a specific program to retrain unemployed persons to perform the profession of seller - the butcher (in Slovenia).	
Absenteeism due to illness	With the implementation of measures and new activities, the company Mercator, d.d., successfully managed the risk of absenteeism due to illness. In the future, this risk is not expected to decline since the burnout and personnel workload increas as a result of rationalization measures and the age structure, which increase the possibility of	In the future, we will continue with the established activities of the project Health promotion (Promocija zdravja) to which we have added some new actions such as: Healthy eating habits week, 5 minutes for well-being in the workplace, Mobility week, A week of safe work – let's prevent slips and falls, Personnel	

	additional injuries. Due to the variable mode of salary payroll in the company Mercator - BH, d.o.o., a positive effect was seen in reducing absenteeism.	priority: 55 + employees management, ... We shall work with physicians of various disciplines, aware employees about healthy lifestyle, promote an active lifestyle through sport-culture club and mountaineering club Mercator, conduct interviews with co-workers who are often absent, implemented emergency medical examinations and check absenteeism when it comes to suspected abuse and report this to management.
Dissatisfaction of employees	In 2012, the introduction of a range of saving measures which have an impact on dissatisfaction with salaries, poor promotion prospects, work organization and greater burden due to optimization of business processes, has led to increased frustration and reduced motivation of employees. At the end of 2012 and in the first quarter of 2013 a reorganization will be in process, which will result in a reduction in labour costs of employees in administration, and will possibly lead to an increase in dissatisfaction.	We shall aware our employees about the necessity of changes to improve operations, which results in the preservation of jobs and a long-term possibility of a pay rise, and opening up opportunities for advancement. In 2013, we shall place great emphasis on the training of leaders at all levels with an aim to improve leadership skills. In Slovenia, we shall begin a discussion with the social partners about a reform of the wage system. We will give emphasis to the importance of variable part of a wage, and as objective methods of assessing the work performance of an individual as possible. We will form a project group that will actively work in the field of communication and interaction with employees, with an aim to reduce the expected overall dissatisfaction due to deteriorating conditions in the labor market.

Legend:

- Risk will decrease
- Risk will remain the same
- Risk will increase

FINANCIAL MANAGEMENT

Stable Financial Operations

Relative to the same period of last year, Mercator Group financial liabilities dropped by 7.5 percent in 2012. As at December 31, 2012 Mercator Group net financial debt amounted to EUR 1,008,034 thousand, which is 7.6 percent less than as at the end of 2011. The decrease is a result of several activities aimed towards deleveraging and establishment of stable ownership structure.

in EUR thousand	Dec.31, 2011	Dec.31, 2012	Index Dec.31, 2012/ Dec.31, 2011
Borrowings and other non-current financial liabilities	822,145	593,841	72.2
Borrowings and other current financial liabilities	362,588	500,879	138.1
Derivative financial instruments (liabilities)	4,562	5,269	115.5
Financial liabilities including derivative financial instruments	**1,189,295**	**1,099,989**	**92.5**
Cash and cash equivalents	27,540	38,012	138.0
Derivative financial instruments (assets)	158	1	0.6
Available-for-sale financial assets	2,628	1,069	40.7
Loans and deposits	67,824	52,873	78.0
Financial assets	**98,150**	**91,955**	**93.7**
NET FINANCIAL DEBT	**1,091,145**	**1,008,034**	**92.4**

Debt-to-Equity Ratio

As at December 31, 2012 Mercator Group attained a debt-to-equity (capital structure) ratio of 1:1.52. The ratio is a quotient between share capital, and net financial debt.

Diversifying the Sources of Financing

Despite the very harsh conditions in financial markets, Mercator Group succeeded in obtaining financing sources from four new international banks or banking groups in 2012, with which the Group had not worked before. Thus, total number of banks or banking groups with which Mercator Group is working now exceeds 30. This strongly reduced the dependence on and exposure to a single bank or banking group, which have recently faced the problems of declining ratings and, as a result, higher price of debt. Four new banking partners are evidence of the trust these institutions have in Mercator as a reliable financial partner.

Issue of short-term commercial papers has become another important financing source. Mercator is one of the first, and currently one of the few companies in the Slovenian market to employ this financing method. As these papers are to a large extent bought by non-banking investors, this further decreases the dependence on the banking sector for financing. In 2012 and early in 2013, Mercator made 4 issues of 6-month commercial papers, amounting from EUR 5 to 12 million.

Mercator, d.d., is one of the first companies in the Slovenian market that chose the issue of short-term corporate commercial papers as one of its financing vehicles.

In the field of debt management and taking into account the increase of refinancing risk in the financial markets, Mercator Group and most banks have reached an agreement on the search for a new long-term liability structure by mid-2013. One of the most important elements of a final agreement, which will be based on the consistency of cash flow available for debt servicing through the financial liabilities, will also be the elimination of refinancing risk, which will increase the financial stability of the Mercator Group.

Current to Non-Current Financial Liability Ratio

As at December 31, 2012, the share of long-term financial liabilities was at 54.2 percent, which is somewhat lower than the target 60% laid down in the Mercator Group financing policy.

Ratio of variable to fixed or hedged financial liabilities

The ratio of variable to fixed or hedged financial liabilities changed in 2012 to the benefit of variable financial liabilities which now account for nearly 54% of all financial liabilities. This is still within the framework of the Mercator Group financing policy which specifies that these should be between 40% and 60% of total financial liabilities.

Available liquidity lines as at December 31, 2012

As at December 31, 2012 Mercator Group had access to the following liquidity lines:

in EUR thousand	**December 31, 2012**
Cash and cash equivalents	38,012
Bank deposits	2,289
Standby revolving credit lines	18,578
Total	**58,879**

Fulfilment of financial commitments and covenants to banking partners

Financial commitments made by the Mercator Group in relation to its lenders are uniform for all financial liabilities and they include three indicators:

- financial leverage indicator (ratio between net financial liabilities and equity),
- interest coverage ratio (ratio between gross cash flow from operating activities/EBITDA and net interest expense), and
- Group equity.

Mercator Group obtained in 2012 a waiver regarding its covenants from all lenders.

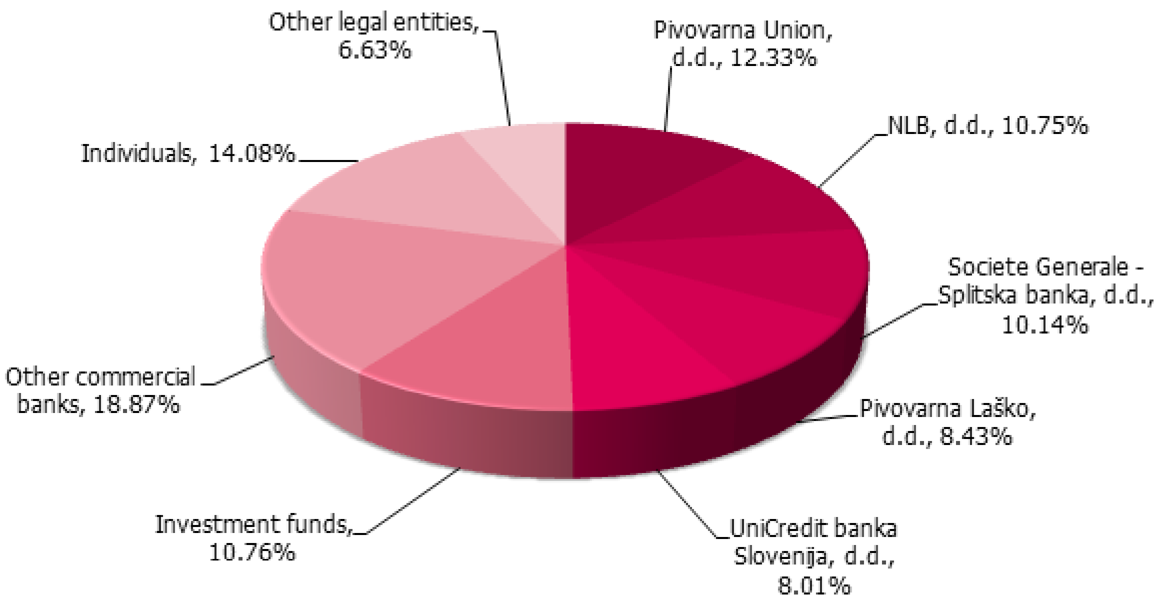
MERCATOR SHARE AND INVESTOR RELATIONS

Mercator share and ownership structure

Basic information on the share of the company Poslovni sistem Mercator, d.d., as at December 31, 2012:

Symbol	MELR
Type	Ordinary share
Listing	Prime market of Ljubljana Stock Exchange, d.d.
Share capital	EUR 157,128,514.53
Number of shares	3,765,361
Number of treasury shares	42,192
Number of shareholders	14,741

Ownership structure of the company Poslovni sistem Mercator, d.d., as at December 31, 2012:



Major Shareholders

As at December 31, 2012, the following ten largest shareholders combined owned **68.84 percent** of the company.

	Major Shareholders	Country	Number of shares	Share
1	Pivovarna Union, d.d.	Slovenia	464,390	12.33%
2	NLB d.d.	Slovenia	404,832	10.75%
3	Societe Generale-Splitska banka, d.d.	Croatia	381,658	10.14%
4	Pivovarna Laško, d.d.	Slovenia	317,498	8.43%
5	UniCredit banka Slovenija, d.d.	Slovenia	301,437	8.01%
6	Nova KBM d.d.	Slovenia	197,274	5.24%
7	HYPO Alpe-Adria bank d.d.	Croatia	158,797	4.22%
8	GB d.d., Kranj	Slovenia	142,920	3.80%
9	Prvi faktor - faktoring, d.o.o., Belgrade	Serbia	125,963	3.35%
10	Radenska, d.d.	Slovenia	96,952	2.57%
		Total	**2,591,721**	**68,84%**

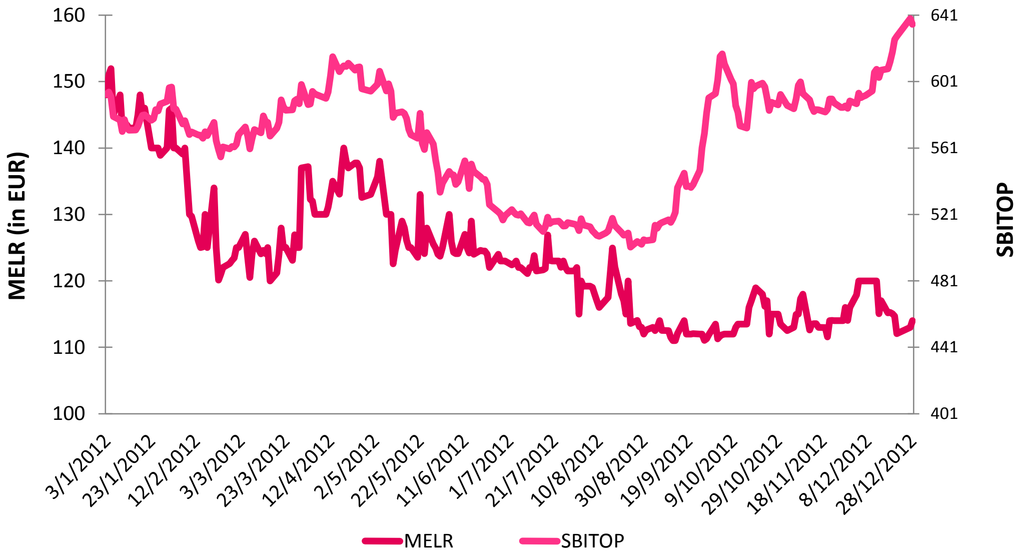
Shares held by Management and Supervisory Board Members as at December 31, 2012

	First and last name	Position	Number of shares	Share
	Management Board			
1	Toni Balažič	Management Board President	0	0.0000%
2	Stanka Pejanović	Senior Vice President	0	0.0000%
3	Drago Kavšek	Senior Vice President	0	0.0000%
4	Igor Maroša	Senior Vice President	0	0.0000%
		Total	**0**	**0.0000%**
	Supervisory Board			
1	Matej Lahovnik	Supervisory Board Chairman	0	0.0000%
2	Rok Rozman	Deputy Supervisory Board Chairman	0	0.0000%
3	Boris Galić	Supervisory Board member	0	0.0000%
4	Zdenko Podlesnik	Supervisory Board member	0	0.0000%
5	Marjeta Zevnik	Supervisory Board member	0	0.0000%
6	Mateja Širec	Supervisory Board member	36	0.0010%
7	Sandi Leban	Supervisory Board member	0	0.0000%
8	Ivan Valand	Supervisory Board member	0	0.0000%
		Total	**36**	**0.0010%**

Foreign shareholders

As at December 31, 2012, the share in the company Poslovni sistem Mercator, d.d., held by foreign investors amounted to **23.49 percent**, which is 6.05 percentage point more than at the end of 2011.

Movement of closing price per MELR share in the period 1-12 2012, compared to the movement of the SBITOP index



Key information for the shareholders

	Dec 31, 2011	Dec 31, 2012	Index
Number of shares registered in Court Register	3,765,361	3,765,361	100.0
Number of treasury shares	42,192	42,192	100.0
Market capitalization (in EUR)	553,508,067	429,251,154	77.6
Market value of share (in EUR)	147.00	114.00	77.6
Book value per share (in EUR)	221.81	198.82	89.6
Minimum close rate in the period (in EUR)	136.00	111.00	81.6
Maximum close rate in the period (in EUR)	182.00	151.95	83.5
Average close rate in the period (in EUR)	162.85	123.46	75.8
Earnings per share (in EUR)	8.4	-20.8	-
Price/earnings ratio (P/E)	17.6	-5.5	-
Capital gains yield (in %)	-6.79	-22.45	-
Dividend yield (in %)	5.07	4.08	80.5
Total yield (in %)	-1.71	-18.37	-

Market capitalization is calculated by multiplying the number of shares entered into the court register as at December 31 with market price per share as at December 31.
Earnings per share is calculated as the ratio between net profit of the company Poslovni sistem Mercator, d.d., and weighted average number of ordinary shares in the period at hand, excluding the treasury shares.
Share book value is calculated as the ratio between the value of the equity of the company Poslovni sistem Mercator, d.d., as at December 31, and the weighted average number of ordinary shares in the period at hand, excluding treasury shares.
P/E (price-to-earnings ratio) is calculated as the ratio between market price per share as at December 31 and net profit per share.
Capital gain is calculated as the ratio between market price per share as at December 31 in the period at hand and market price per share as at December 31 in the previous period.
Dividend yield is calculated as the ratio between dividend per share and market price per share as at December 31.

Dividend policy

In 2012, the company Poslovni sistem Mercator, d.d., pay dividends in the amount of EUR 6.00 per ordinary share.

The Management Board together with the Supervisory Board each year considers the appropriateness of the amount of dividends in relation to the business and financial factors, their payout is decided by the General Meeting.

Treasury shares

As at December 31, 2012, the company Poslovni sistem Mercator, d.d., held 42,192 treasury shares. In the period 1-12 2012, the company neither acquired nor disposed of treasury shares.

Investor relations

Relation with all the stakeholders is based on ensuring transparency of our operations, which is achieved by regular and timely announcement of information on the company status and position, as well as on major changes in company operations. Information are published on the website www.mercator.si and the system of electronic communication of Ljubljana Stock Exchange, SEOnet, in which all releases and announcements have also been published in English since 2005.

Mercator treats all shareholders holding shares of the same class equally, and motivate them to exercise their rights proactively and responsibly.

The company motivates major shareholders and institutional investors to publicly disclose their investment policy at the company, e.g. their voting policy, level of activity in the corporate governance process and the manner thereof, and the mechanisms and frequency of communication with the managerial or supervisory bodies.

Mercator also regularly organizes meeting with shareholders at the company headquarters, press conferences on major business events and announcements of business results, meetings with investors and analysts, presentation meetings and conferences for investors at home and abroad.

SUSTAINABILITY REPORT

In 2012, our sustainability efforts were focused, economic conditions permitting, on all fields of the concept of sustainable development of a society. In particular, we were focused on activities that result in decrease of costs, and activities related to the needs of our customers.

RESPONSIBILITY TO CUSTOMERS

Care for food safety

Consumers are at the heart of Mercator's effort. Therefore, responsibility to consumers comes first. Our mission is to see our customers satisfied, recognizing us as the best retailer offering everything a discount store can offer, and much more. The key medium-term goals in responsibility to customers are to provide efficient annual internal control over each unit and appointment of a permanent expert team for control of quality and safety of the Mercator private label. In 2012, we thus carried out 578 regular and 24 extraordinary controls at our stores. In order to offer our consumers safe and quality food, we analyzed 1,498 samples of private label products; monitored 1,760 samples in open departments; and recorded 364 samples as a part of the national monitoring.

A lot of attention is devoted to constant monitoring and control of quality of all private label products. In 2012, we analyzed 1,498 samples of private label products.

Introduction of new standards and environmentally friendly technologies

By employing technologically efficient refrigeration equipment, we saved over EUR 400 thousand.

The use of technologically efficient refrigeration equipment is aimed towards the reduction of the use of electricity at our stores. In 2012, we reduced our power consumption by 1% by introducing modern refrigeration equipment. By installing doors on the refrigeration equipment elements at 50 stores, we saved over EUR 400 thousand.

We are looking to standardize particular solutions of sustainable development and to upgrade the existing Mercator Standards. Standardized elements are included in the sales network. Thus, we added shopping carts made of recycled materials at newly built and opened hypermarkets, as well as more efficient refrigeration equipment and lighting, which led to a reduction in power consumption relative to other comparable facilities by 2%.

Marketing activities related to the offer of environmentally friendly products and services

We are pursuing the goal of consistent use of new communication solutions for environmentally friendly offer and services especially in stores and in digital media.

In the second half of 2012, we redesigned the local offer at Mercator stores in Slovenia, added a slogan, and merged it into a single line **"Iz domačih krajev"** (locally produced/from the countryside). The campaign initially involved offering the customers Slovenian fruit and vegetables at over 100 marketplaces located in Mercator's larger stores. We continued the campaign by selecting the typical bread for each Slovenian region, followed the tradition of country feasts with pork and offer of fresh meat produced and farmed in Slovenia. At the end of the year, we prepared a special offer of regional sorts of wines.

RESPONSIBILITY TO EMPLOYEES

Number of employees

MARKET	**Number of employees as at Dec. 31, 2011**	**Number of employees as at Dec. 31, 2012**	**Index Number of employees Dec. 31, 2012/ Dec. 31, 2011**	**Number of employees based on hours worked in the period 1-12 2012**
Slovenia	12,034	11,794	98.0	11,230
Serbia	4,806	4,764	99.1	4,586
Croatia	3,873	3,627	93.6	3,316
Bosnia and Herzegovina	1,722	2,004	116.4	1,855
Montenegro	1,429	1,417	99.2	1,481
Bulgaria	268	205	76.5	194
Albania	134	109	81.3	107
TOTAL	**24,266**	**23,920**	**98.6**	**22,769**

Highly trained employees are our key competitive advantage; in 2012, we devoted extra attention to them.

We revised the competencies and carried out leader evaluation. In addition, we sent competence profiles to all leaders and their superiors; these profiles were the central topic of this year's annual interviews. Furthermore, we organized Shop manager training at the company Poslovni sistem Mercator, d.d., and at all trade companies in Southeastern Europe.

Development of leadership skills, training and education, motivation and rewards to employees, and recruitment

We held 22 team-building workshops on Vogel. In Southeastern European markets, we organized Crash courses on management and prepared the program for the first School for future leaders.

We successfully completed the first Mercator's stock assistant training which took place in Slovenia.

HRM strategy included developing the so-called generation management consisting of two parts: management of employees aged 55 and above (55+), and 30 and below (30-).

We also developed a standard for the corporate system of internal instructors which, among other effects, promotes training of new internal instructors. 1,288 internal instructors at Mercator Group were presented standardized certificates. Another major addition is the development of e-library called Mercator's growing book.

We set up an e-classroom on the intranet, which will allow the employees a fast, inexpensive, and user-friendly approach to our training and education materials.

This year, Mercator Award was presented to 22 employees. In addition, we held the Best Boss survey for the sixth consecutive year, and presented awards to the best bosses.

Dialogue with the employees and social partners; occupational health and safety

We organized an open day door in Naklo and at the headquarters of Mercator, d.d., for the children of our employees. In Slovenia, we presented Lumpi packages to 275 parents of newborn babies.

Approximately 1,500 key employees attended the 6th Key Employee Council at which the new Management Board was presented.

We used a special application for classified ads to allow our employees to exchange various items and objects through Mercator's intranet, the GIVEAWAY Portal. Thus, we encouraged mutual solidarity.

Mercator Humanitarian Foundation provided a total of EUR 73 thousand of aid to 133 employees that were ill or in social distress.

RESPONSIBILITY TO NATURAL ENVIRONMENT

Reducing power consumption and heating fuel

Efficient use of energy has become a part of Mercator's comprehensive corporate social responsibility. In addition to energy management, it involves environmental aspects, process aspects, and aspects of business performance. Mercator trade centers are constructed according to the principle of energy-efficiency. In our decisions, we also favour the use of alternative sources of energy. Mercator's goals regarding energy efficiency are consistent with the adopted National Action Plan for energy efficiency until the year 2016.

As the prices of fossil fuels grow, investments in alternative energy sources are increasingly viable. Lower dependence on fossil fuels, the prices of which are mounting, means lower and more predictable energy costs. Therefore new alternative systems are being monitored and implemented at Mercator as well. These systems are intended to promote environmental awareness, reduce the load on the environment, and improve business performance, competitiveness, and productivity of the company. Co-generation, or combined heat and power (CHP), is a method to improve the use of fuel by reaping both heat and electric energy generation simultaneously. Such technology has been installed at nine units in Slovenia. Compared to separate generation where additional losses are caused by transfer through power lines, equipment of such type delivers notably higher yield and considerably decreases the effect on the environment (e.g. greenhouse emissions etc.).

Due to effects on the environment and lower consumption of primary energy, the European Union started to promote the proliferation of such systems by providing government grants or operation support.

Thus, installation of nine co-generation systems resulted in positive effects on the environment, as well as annual energy cost savings of approximately EUR 150 thousand per year.

Cutting the use of natural resources and waste generation

The cost of packaging fee and environmental taxes and charges for waste packaging were reduced by EUR 459 thousand.

We are striving for continuous waste separation activities pursuant to relevant legislation, and to set up waste records. In order to meet the medium-term plan of reducing the amounts of mixed municipal waste by 10%, we reduced the size of containers for mixed solid municipal waste at 10 stores. We also reduced the cost of packaging fee and environmental taxes and charges for waste packaging by EUR 459 thousand.

We set up a central entry point for reporting extraordinary events in environment protection (generation of a large amount of hazardous waste; chemicals spill; flooding etc.) an d calculated the carbon footprint for the company, the store, and Mercator private label product.

RESPONSIBILITY TO SOCIAL ENVIRONMENT

Donations and sponsorships

In 2012, we supported over 1,600 projects in the region with sponsorships and donations.

Sponsorships and donations are an important vehicle for our contribution to areas that matter the most to the society and the people, which will improve the quality of life and satisfaction of the people. Our activities contribute to the development of the local (regional) economy, and social development. Also a part of our corporate social responsibility efforts are the humanitarian campaign, sponsorships and donations, educational, cultural, and healthcare activities.

Major project carried out in 2012 include the following:

- donation of food to Slovenian Caritas;
- participation in the Slovenian Red Cross campaign "Let's take them to the seaside";
- donation of gift certificates to the Friends of the Youth Association Moste Polje for families in social distress;
- aid to the Okrešelj Foundation for the children of fatally injured rescue team members;
- donation of products to Slovenian maternity homes;
- donation of fruit to children's homes in Croatia;
- aid to the safe house in Pilštanj;
- Slovenian drama week in Kranj;
- golden subscription at the Cankarjev Dom;
- concert of opera arias as a part of the Ljubljana Festival;
- Dragon's Children's Games Festival in Novi Sad;
- support to activities of the Co-habitation society "Healthy Food" - contest on healthy nutrition for kindergartens and schools;
- sponsoring the "Are we understood?" experiment at the House of Experiments;
- national competition of high-school students in sales techniques;
- final event of the clean teeth competition;
- tour of Slovenia bicycle race;
- hike along the wire;
- run for hope, organized by EuropaDonna;
- Ljubljana marathon;
- Olympic Committee of Slovenia and Serbia.

Despite the harsh conditions which Mercator was faced with and despite all adopted measures of cost rationalization, donations and sponsorships remain important activities that contribute to the improvement of the situation in the society.

RESPONSIBILITY TO SUPPLIERS

Relations with suppliers

Particular attention is paid to operations with proven suppliers, selection of assortment, pricing, promotions, and training and education of both employees at the stores and consumers. As a responsible business partner, we nurture long-term respectful relations with our suppliers. Therefore, we are working on obtaining in the coming years from all suppliers that we work with signed statements of safety, product quality, compliance of food and materials, respect for human rights, and relation to the broad environment.

Mercator farmer's markets also include over 100 small growers and farmers' cooperatives.

In 2012, we offered our customers 410 local, home-made products by 80 local suppliers. The offer of Mercator Marketplace includes products of over

100 small growers and farmers' cooperatives, including 120 different types of Slovenian fruit and vegetables.

We signed supply agreement with Slovenian farmers and small growers for 2013, which will allow us to increase the purchase of Slovenian fruit and vegetable by 5% relative to the year 2012.

Establishing global supply will be an important process in the coming period as it will allow us to focus on the purchasing and sourcing synergies for particular categories and to reap market synergies. Our offer will also include products by new suppliers. Special attention will be paid to other important links in the chain: farmer's associations, farmers' cooperatives, and packaging manufacturers, which are all promoted to offer joint support to local Slovenian growing. We shall increase the revenue of both the Mercator Group and the suppliers by cooperating more closely and by connecting the markets, as well as by increasing the value added for the consumer.

RESPONSIBILITY TO QUALITY

Maintenance, implementation, and certification of international quality management systems

By efficient management of business processes and quality of products and services, we are fostering long-term trust of all our stakeholders. In our comprehensive quality management, we apply international quality standards and the principles of business excellence, and we conduct regular and follow-up audits of the existing certified quality management systems.

Mercator Group currently holds 15 active quality certificates.

In 2012, we ceased to certify the standards ISO 22000 at Mercator, d.d., and HACCP at Mercator–S, d.o.o. Instead, three additional standards are being certified: ISO 9001, AIB International Consolidated Standard, and SQMS Supplier Quality Management System at the manufacturing company Mercator - Emba, d.d.

Management of documents, records, non-compliance, and measures

Mercator Standards collection currently includes 3,045 valid documents. In 2012, we published 970 new or revised documents; 80 documents were archived.

We are operatively managing any non-compliance and carrying out corrective and preventive measures. In the second half of 2012, we used a new application to document 45 applications.

Systemic monitoring of quality management processes

Systemic monitoring of processes and quality management includes defining the key indicators and monitoring the proposed measures. In 2012, we monitored and analyzed environmental indicators for individual environmental aspects at Mercator Group companies.

In 2012, the following applies to nine companies of the Mercator Group:

- energy costs amounted to EUR 43.8 million (which is 2% more than in 2011); specific energy cost amounted to EUR 25.52 per m^2;
- carbon dioxide emissions of fuels amounted to 267,709 tons of CO_2 (which is 6% lower than in 2011); specific emissions amount to 156 kg CO_2/m^2;
- power consumption amounted to 408.19 GWh (which is 6% less than in 2011); specific power consumption was at 237.97 kWh/m^2.

FINANCIAL REPORT

FINANCIAL REPORT OF THE MERCATOR GROUP

Consolidated balance sheet

EUR thousand	Note	Dec 31, 2012	Dec 31, 2011 restated	Jan 1, 2011 restated
ASSETS				
Non-current assets				
Property, plant and equipment	14	1,874,735	1,906,018	1,870,428
Investment property	16	3,194	3,450	3,894
Intangible assets	15	18,387	35,862	52,626
Deferred tax assets	19	20,378	12,774	11,674
Loans and deposits	22	50,034	65,823	77,113
Available-for-sale financial assets	17	1,069	2,628	3,959
		1,967,797	**2,026,555**	**2,019,694**
Current assets				
Inventories	20	267,711	309,941	297,013
Trade and other receivables	21	239,998	243,402	231,871
Current tax assets		6,462	4,062	-
Loans and deposits	22	2,839	2,001	17,346
Derivative financial instruments	18	1	158	70
Cash and cash equivalents	23	38,012	27,540	20,766
		555,023	**587,104**	**567,066**
Total assets		**2,522,820**	**2,613,659**	**2,586,760**
EQUITY	24			
Share capital		157,129	157,129	157,129
Share premium		198,872	198,872	198,872
Treasury shares		(3,235)	(3,235)	(3,235)
Revenue reserves		197,045	264,310	248,736
Fair value reserve		240,762	192,209	200,187
Retained earnings		(21,714)	10,294	6,671
Profit (loss) for the year		(26,953)	(3,068)	30,396
Currency translation reserve		(78,819)	(60,275)	(62,295)
Total equity attributable to equity owners of the Company		**663,087**	**756,236**	**776,461**
Non-controlling interests		**162**	**221**	**243**
Total equity		**663,249**	**756,457**	**776,704**
LIABILITIES				
Non-current liabilities				
Trade and other payables	28	2,462	2,369	2,447
Borrowings and other financial liabilities	26	593,841	822,145	674,375
Deferred tax liabilities	19	52,640	48,845	51,269
Provisions	27	31,459	32,711	35,709
		680,402	**906,070**	**763,800**
Current liabilities				
Trade and other payables	28	672,858	583,982	642,666
Current tax liabilities		163	-	5,259
Borrowings and other financial liabilities	26	500,879	362,588	395,853
Derivative financial instruments	18	5,269	4,562	2,478
		1,179,169	**951,132**	**1,046,256**
Total liabilities		**1,859,571**	**1,857,202**	**1,810,056**
Total equity and liabilities		**2,522,820**	**2,613,659**	**2,586,760**

Consolidated income statement

EUR thousand	Note	2012	2011 restated
Revenue	9	2,873,186	2,870,971
Cost of goods sold and selling costs	11	(2,745,203)	(2,704,991)
Administrative expenses	11	(130,416)	(96,855)
Impairment of property, plant and equipment and intangible assets	11	(59,842)	(16,438)
Other income	10	20,128	24,154
Results from operating activities		**(42,147)**	**76,841**
Finance income	13	4,779	5,699
Finance expenses	13	(72,911)	(62,600)
Net finance expense		**(68,132)**	**(56,901)**
Profit (loss) before tax		**(110,279)**	**19,940**
Tax expense	19	5,659	(7,451)
Profit (loss) for the year		**(104,620)**	**12,489**
Profit (loss) for the year attributable to:			
Owners of the parent company		(104,555)	12,506
Non-controlling interests		(65)	(17)
Basic and diluted earnings per share (in EUR)	25	(28.1)	3.4

Consolidated statement of comprehensive income

EUR thousand	Note	2012	2011 restated
Profit (loss) for the year		**(104,620)**	**12,489**
Other comprehensive income			
Foreign currency translation differences - foreign operations		(18,544)	2,015
Change in fair value of available-for-sale financial assets	24	(89)	(1,208)
Disposal of available-for-sale financial assets reclassified to profit or loss	24	699	-
Change in fair value of cash flow hedges	24	(864)	(2,780)
Revaluation of property	24	55,145	-
Deferred taxes	19	(2,596)	978
Other comprehensive income for the year		**33,751**	**(995)**
Total comprehensive income for the year		**(70,869)**	**11,494**
Total comprehensive income for the year attributable to:			
Owners of the parent company		(70,810)	11,516
Non-controlling interests		(59)	(22)

Consolidated statement of changes in equity

EUR thousand	Note	Share capital	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Profit (loss) for the year	Currency translation reserve	Total equity attributable to owners of the parent company	Non-controlling interests	Total equity
Balance at January 1, 2011		**157,129**	**198,872**	**(3,235)**	**270,194**	**200,187**	**6,671**	**30,396**	**(62,295)**	**797,919**	**246**	**798,165**
Impact of changes in accounting policies	2(e)	-	-	-	(21,458)	-	-	-	-	(21,458)	(3)	(21,461)
Restated balance at January 1, 2011		**157,129**	**198,872**	**(3,235)**	**248,736**	**200,187**	**6,671**	**30,396**	**(62,295)**	**776,461**	**243**	**776,704**
Total comprehensive income for the year												
Profit for the year		-	-	-	-	-	-	12,506	-	12,506	(17)	12,489
Other comprehensive income		-	-	-	-	(6,022)	3,012	-	2,020	(990)	(5)	(995)
Total comprehensive income for the year		**-**	**-**	**-**	**-**	**(6,022)**	**3,012**	**12,506**	**2,020**	**11,516**	**(22)**	**11,494**
Transactions with owners of the parent company directly recognized in equity												
Contributions by and distributions to owners												
Dividends to equity holders*		-	-	-	-	-	(29,785)	-	-	(29,785)	-	(29,785)
Total contributions by and distributions to owners		**-**	**-**	**-**	**-**	**-**	**(29,785)**	**-**	**-**	**(29,785)**	**-**	**(29,785)**
Changes in ownership interests in subsidiaries												
Disposal of subsidiary		-	-	-	-	(1,956)	-	-	-	(1,956)	-	(1,956)
Total transactions with owners of the parent company		**-**	**-**	**-**	**-**	**(1,956)**	**(29,785)**	**-**	**-**	**(31,741)**	**-**	**(31,741)**
Transfer of profit of the previous year to retained earnings	24	-	-	-	-	-	30,396	(30,396)	-	-	-	-
Distribution of profit for the year pursuant to Management Board/Supervisory Board decision	24	-	-	-	15,574	-	-	(15,574)	-	-	-	-
Restated balance at December 31, 2011		**157,129**	**198,872**	**(3,235)**	**264,310**	**192,209**	**10,294**	**(3,068)**	**(60,275)**	**756,236**	**221**	**756,457**

* The amount of dividend payment differs from the amount specified in the Shareholders Assembly resolution because treasury shares were included in the calculation of the required amount for dividend payment.

Consolidated statement of changes in equity (continued)

EUR thousand	Note	Share capital	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Profit (loss) for the year	Currency translation reserve	Total equity attributable to owners of the parent company	Non-controlling interests	Total equity
Restated balance at January 1, 2012		**157,129**	**198,872**	**(3,235)**	**264,310**	**192,209**	**10,294**	**(3,068)**	**(60,275)**	**756,236**	**221**	**756,457**
Total comprehensive income for the year												
Profit (loss) for the year		-	-	-	-	-	-	(104,555)	-	(104,555)	(65)	(104,620)
Other comprehensive income		-	-	-	-	48,553	3,736	-	(18,544)	33,745	6	33,751
Total comprehensive income for the year		**-**	**-**	**-**	**-**	**48,553**	**3,736**	**(104,555)**	**(18,544)**	**(70,810)**	**(59)**	**(70,869)**
Transactions with owners of the parent company directly recognized in equity												
Contributions by and distributions to owners												
Dividends to equity holders*		-	-	-	-	-	(22,339)	-	-	(22,339)	-	(22,339)
Total transactions with owners of the parent company		**-**	**-**	**-**	**-**	**-**	**(22,339)**	**-**	**-**	**(22,339)**	**-**	**(22,339)**
Transfer of profit (loss) of the previous year to retained earnings	24	-	-	-	-	-	(3,068)	3,068	-	-	-	-
Distribution of revenue reserves pursuant to Management Board decision	24	-	-	-	(67,265)	-	(10,337)	77,602	-	-	-	-
Balance at December 31, 2012		**157,129**	**198,872**	**(3,235)**	**197,045**	**240,762**	**(21,714)**	**(26,953)**	**(78,819)**	**663,087**	**162**	**663,249**

* The amount of dividend payment differs from the amount specified in the Shareholders Assembly resolution because treasury shares were included in the calculation of the required amount for dividend payment.

Consolidated statement of cash flows

EUR thousand	Note	2012	2011 restated
Cash flows from operating activities			
Profit (loss) for the year		**(104,620)**	**12,489**
Adjustments:			
Income tax expense	19	(5,659)	7,451
Depreciation of property, plant and equipment	14	74,097	71,745
Depreciation of investment property	16	140	160
Amortisation of intangible assets	15	7,552	9,401
Impairment of goodwill	15	5,885	3,037
Impairment of property, plant and equipment, intangible assets and (gain) loss on sale of property, plant and equipment	10,11	51,899	6,578
Change in provisions and deferred income	27	9,881	(677)
Gains on sale of subsidiaries	13	-	(1,150)
Dividends received, impairment losses and (gain) loss on sale of available-for-sale financial assets	13	366	(29)
Excess of acquirer's interest in the net fair value of acquiree's identifiable assets and liabilities over cost	8	(1,349)	(118)
Net foreign currency translation	13	9,363	3,383
Interest received	13	(3,374)	(3,647)
Interest paid	13	50,939	53,879
		95,120	**162,502**
Change in inventories		42,527	(16,202)
Change in trade and other receivables		92	(19,027)
Change in trade and other payables		78,391	(66,540)
		216,130	**60,733**
Interest paid	13	(50,939)	(53,879)
Income tax paid	19	(144)	(8,573)
Net cash from (used in) operating activities		**165,047**	**(1,719)**
Cash flows from investing activities			
Acquisition of subsidiaries and business operations, net of cash acquired	8	(390)	(7,706)
Acquisition of property, plant and equipment and investment property	14,16	(62,948)	(111,024)
Acquisition of intangible assets	15	(4,382)	(4,800)
Aquisitions of available-for-sale financial assets	17	(9)	(10)
Loans and bank deposits made		(839)	(1,481)
Disposal of subsidiaries, net of cash disposed of		-	9,985
Proceeds from sale of property, plant and equipment and investment property	14,16	7,292	17,228
Proceeds from sale of intangible assets	15	16	1
Proceeds from sale of available-for-sale financial assets	17	1,701	-
Interest received	13	3,374	3,647
Dividends received	13	113	56
Loans and deposits repayments received		15,796	28,585

Net cash used in investing activities		**(40,276)**	**(65,519)**
Cash flows from financing activities			
Repayment of non-current borrowings	26	(257,124)	(203,387)
Increase in non-current borrowings	26	28,218	350,013
(Repayment) increase in current borrowings	26	137,876	(42,836)
Dividends paid		(22,163)	(30,038)
Net cash from (used in) financing activities		**(113,193)**	**73,752**
Net increase in cash and cash equivalents		**11,578**	**6,514**
Cash and cash equivalents at the beginning of the year		27,540	20,766
Effect of exchange rate fluctuations on cash and cash equivalents held		(1,106)	260
Cash and cash equivalents as at the end of the year	23	**38,012**	**27,540**

Notes to consolidated financial statements

1. Reporting company

Poslovni sistem Mercator, d.d. (hereinafter referred to as Mercator, d.d.), is a company headquartered in Slovenia. The address of its registered head office is Ljubljana, Dunajska cesta 107. The consolidated financial statements of the Mercator Group as at and for year ended December 31, 2012 comprise the company Mercator, d.d., and its subsidiaries (together referred to as the "Group"). The Group's core and predominant activity is retail and wholesale of fast-moving consumer goods and home products; to a lesser extent, the Group is active in production of alimentary products.

2. Basis of preparation

(a) Statement of compliance

Consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU, and in compliance with the provisions of the Slovenian Companies Act.

Consolidated financial statements were approved by the Company Management Board on February 4, 2013.

(b) Basis of measurement

Consolidated financial statements have been prepared on the historical cost basis, except for the items listed below:

- derivative financial instruments measured by fair value;
- available-for-sale financial assets at fair value;
- real property valued according to the revaluation model.

The methods used to measure fair values are discussed further in Note 5.

The Management Board was in the process of negotiations with its banking partners because the Group failed to attain at the end of the first half of 2012 and as at December 31, 2012 the minimum value of the interest coverage ratio (ratio between gross cash flow from operating activities (EBITDA) and net interest expense), and exceeded the maximum value of the financial leverage indicator (ratio between net financial liabilities and equity). The Management Board was granted waivers for these covenants.

(c) Functional and presentation currency

The consolidated financial statements attached herewith are presented in EUR, i.e. in the functional currency of the company Poslovni sistem Mercator, d.d. All financial information figures presented in EUR are rounded to one thousand units.

(d) Use of estimates and judgements

Preparation of financial statements in compliance with the IFRS requires the company management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

In particular, information about significant areas of uncertainty regarding estimation and critical judgements in applying accounting policies that have the most significant effect on the amounts recognized in the financial statements is given below.

(i) Goodwill

Each year, impairment test is conducted by the Group concurrently with the compilation of financial statements. Upon acquisition, goodwill was allocated to groups of cash-generating units represented by clusters of comparable entities such as Mercator centers, hypermarkets, supermarkets, and smaller units. Recoverable amount of the cash-generating unit is specified based on the calculations of value in use, or fair value minus the selling costs. Calculations include projections of cash flows based on the business plans adopted by the Management Board for the following year, and on the expected operating results in the coming medium-term period, based on the assumptions and policies specified in the medium-term business plan for each company and therefore the Mercator Group as a whole. The Management Board has prepared projections based on the business performance record (history) and expectations with regard to development of the market. The discount rate applied is based on market rates adjusted to reflect the specific risks related to the business units.

(ii) Accounting for borrowing costs

In respect of borrowing costs relating to qualifying assets, the Group, pursuant to IAS 23 Borrowing Costs (2007), capitalizes borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. Capitalization of interest expense is performed for major investments whose construction and preparation for use lasts more than 6 months. In 2012, no investment meets the above criteria for capitalization of borrowing expenses.

(iii) Available-for-sale financial assets

The Group's long-term financial investments into equity of other companies, classified as available-for-sale financial assets, also include such assets that could not be appraised at fair value. Shares of these companies are not listed or traded in the stock market. Fair values of these assets cannot be reliably measured; therefore, they are valued by historical cost.

(iv) Trade and other receivables

Provision for the impairment of trade and other receivables is based on pending legal processes and previous years' experience. The estimate is based on the assumption that trade and other receivables will be paid in recognized amount.

Receivables with quality insurance (backed by security) shall be exempt from the calculation of revaluation adjustment. Revaluation adjustments for short-term trade receivables and receivables related to purchases with the Mercator Pika card shall be recognized according to the age of the receivables. Thus, the value of trade receivables and default interest in this regard shall be adjusted by 50% if the receivable is overdue by 61 to 74 days; 75% if the receivable is overdue by 75 to 89 days; and by 100% if the receivable is overdue by 90 days or more. Short-term receivables from Pika card holders shall be adjusted by 100% if the receivables are overdue by 90 days or more.

Disputed receivables (lawsuit, bankruptcy, compulsory composition) shall be adjusted by 100%.

Revaluation adjustments to other receivables shall be made individually.

(v) Inventories

Carrying values of inventories do not exceed their realizable value in all material aspects. Allowances and write-downs of inventories are based on previous years' experience.
General rule:

- value of inventory acquired a year before the current year shall be adjusted by 50% of their cost;
- value of inventory acquired two years or more before the current year shall be adjusted by 80% of their cost;

Exceptions:

- Value of inventory at Beautique units shall only be adjusted when it is older than two years. Then, the value shall be adjusted by 80%.
- Value of inventory at Intersport stores shall only be adjusted when it is older than two years. Then, the value shall be adjusted by 50%.

In the future, the Group does not expect any events that would significantly influence the accounting estimates.

(vi) Provisions

Carrying values of provisions are measured as the present value of the expenditures expected to be required to settle the obligation. Estimates are given by experts, or the values are based on original documentation. The outcome and the date of resolution of legal proceedings which were the basis for recognition of provisions are uncertain. In the future, the Group does not expect any events that would significantly influence the accounting estimates.

Retirement benefits and jubilee premium provisions refer to estimated payments of retirement benefits and long service awards presented to the employees who have been with the Group for a long period of time, as at the reporting date, discounted to present value. These provisions have been made for expected payments. Calculation of the figure also accounted for the expected growth of wages from the day of the calculation until the day of retirement of a particular employee, as well as employee fluctuation. Salary growth consists of career promotion and the related wage inflation. To calculate the present value of retirement benefits and jubilee premium provisions, a discount rate was used that is equal to the market yield on highly rated euro-denominated corporate bonds (see note 3(j) (i)).

In the future, the Group does not expect any events that would significantly influence the accounting estimates.

(vii) Deferred tax

Deferred income taxes are calculated on all temporary differences under the liability method using a tax rate which will enter into force in next financial year. If the tax rate changes, the deferred income tax assets and liabilities will change appropriately.

Mercator Group companies shall recognize deferred tax assets for transfer of unused tax losses and unused tax credit to the following period only in cases when it is likely that future taxable income is available against which the unused tax losses and unused tax credits can be charged. The basis for estimate is Mercator Group's medium-term business plan.

In the future, the Group does not expect any events that would significantly influence the accounting estimates.

(e) Changes to accounting policies, correction of error from previous years, and other adjustments of financial statements

(i) Introduction

In 2012, the Mercator Group changed its accounting policy with regard to the accounting for merchandise inventories and the method of calculating the cost of the goods sold.

An error was made at the company Mercator - S, d.o.o., at the end of the year 2011 when the fair value was revised of an intangible asset recognized based on a long-term lease agreement for retail units under terms more favourable than the market conditions, because the fair value calculation model failed to adjust the key assumption on the market rent value. These rents dropped significantly in 2011.

Business combination of companies Mercator - BH, d.o.o., Sarajevo, and Drvopromet, d.o.o., Sarajevo was carried out at the end of 2011; however, the takeover of DP Marketi business units and further analysis of their customers led to important new discoveries and conclusions based on which a re-assessment of this strategic combination was made.

After a detailed analysis of contracts made with the suppliers of merchandise, and of the interdependence between their contents and the quantities supplied, we reclassified some rebates and compensations to allow for better comparison of the 2012 financial statements with those from the previous year.

(ii) Changes in accounting policies

Pursuant to the provisions of Article 7 of the Code of Practice for the stakeholders in the agrifood chain, adopted in 2011, Mercator Group changed on January 1, 2012 the way it manages its relations with majority of suppliers of fast-moving consumer goods in Slovenia, by implementing pricing according to net-net price system. Therefore, all rebates and other discounts that were previously reported for the entire period are now reported in current purchasing transactions, which results in a lower value of inventory. At the same time, the value of rebates and other discounts is reported as a decrease in the cost of goods sold rather than being reported in revenue.

In addition to the transition to net-net pricing, Mercator Group companies in Slovenia changed, due to gradual implementation of standardized IT systems in retail and warehouse units, which started during 2011 and which will presumably be completed by the first half of 2013, the way of calculating and reporting the cost of goods sold from calculation method to the actual method.

The table below shows the adjustments to the balance sheet as a result of the implementation of the new accounting policy and the change in the method of calculating the cost of goods sold:

EUR thousand	Inventories	Deferred tax assets	Revenue reserves	Profit (loss) for the year	Non-controlling interest	Current tax liabilities	Current tax assets
Effect of the change in accounting policy at January 1, 2011	(25,068)	2,974	(21,458)	-	(3)	(633)	-
Effect of the change in accounting policy in 2011	(240)	(37)	-	(275)	-	126	128

Effects of all changes described above on the income statement for last year amount to EUR -275 thousand: cost of goods sold rose by EUR 240 thousand, and income tax rose by EUR 35 thousand. All changes described above were carried out in compliance with IAS 8 – Accounting Policies, Changes in Accounting Estimates and Errors. This means that the opening balances of relevant items of equity for the year 2011, and all other comparative amounts disclosed in the previous periods, were re-calculated as if the changed accounting policy had been used since the start. Although the Group results (net income) decreased as a result, tax liabilities increased. In 2011, some companies ran a net loss, or they used tax reliefs and therefore did not recognize or pay income tax. Increase of tax liabilities mostly occurred at the parent company where results for 2011 were improved as a result of the change in policy.

(iii) Correction of error

In 2006, the company Mercator – S, d.o.o recognized in its books an intangible asset on the basis of a long-term preferential lease obtained from company Rodić MB Trgovina (i.e. long-term lease of retail units under terms more favourable than the market conditions, which brings the company long-term economic benefit). Later, these business units were exchanged for others (C&C Zmaj Beograd, SM Požega, SM Pančevo, SM Sremska Mitrovica, SM Novo Naselje - Novi Sad), equally under terms more favourable than the market conditions.

In 2011, market rents in Serbia plummeted; so much so that previously much more favourable rents became equal to market rents. The company carried out the impairment test already in 2011; however, impairment was not made due to erroneous calculation. The error was discovered in 2012; therefore, the company repeated the test and established the need for impairment which was recorded in the fiscal year 2011.

The following table shows the adjustments to the balance sheet resulting from the correction of error:

EUR thousand	Intangible assets	Deferred tax liabilities	Profit(loss) for the year
Effect of accounting error in 2011	(9,851)	985	(8,866)

Effects of all changes described above on the income statement for last year amount to EUR -8,866 thousand: impairment of intangible assets rose by EUR 9,851 thousand, and income tax expenses (deferred taxes) dropped by EUR 985 thousand.

(iv) Other adjustments

Change in accounting for business combinations

In case of business combinations IFRS 3 Business Combinations allows companies a one-year horizon for the assessment of and possible change in its accounting.

The company Mercator - BH, d.o.o., Sarajevo, and the company Drvopromet, d.o.o., Sarajevo, signed an agreement on strategic combination, according to which Mercator - BH, d.o.o., took over the trade operations of the company Drvopromet, d.o.o. The takeover was carried out in two successive stages: 36 units were taken over in 2011, and the remaining units were taken over in January 2012.

Due to the takeover, a fair value adjustment in the amount of EUR 1,910 thousand was recognised in financial statements for the year 2011. It referred to the capitalization of the »Drvopromet« brand. The Group de-recognized the excess of the acquirer's interest over the cost of the business combination in the amount of EUR 1,910 thousand through profit or loss of 2011.

After Drvopromet markets were taken over, further analyses of their customers led to important new discoveries and conclusions. The customer loyalty analysis in Drvopromet markets has shown that buyers are not loyal to the Drvopromet brand; price, supply range, quality of services, location, and other factors are important to them. Consequently, it was established that the value of the Drvopromet brand, recognized at the date of accounting for the business combination, was overvalued.

In compliance with the possibilities provided by IFRS 3 in relation to the accounting of business combinations, the value of the strategic combination was reassessed.

EUR thousand	**Pre-acquisition carrying amounts**	**Fair value adjustments**	**Recognized values on acquisition**
Property, plant, and equipment	1,555	-	1,555
Intangible assets	-	-	-
Inventories	1,606	-	1,606
Net identifiable assets and liabilities	**3,161**	**-**	**3,161**
Excess of acquirer's interest in the net fair value of acquiree's identifiable assets and liabilities over cost			**-**
Consideration			3,161
Obtained cash			-
Cost of acquisition less obtained cash			3,161

The change in the accounting of the strategic combination affects the financial statements for the year 2011 in that the recognized intangible asset has been de-recognized in its total amount of EUR 1,910 thousand, and the profit (loss) for the year has been decreased.

EUR thousand	**Intangible assets**	**Profit (loss) for the year**
Effect of change of value of business combination in 2011	(1,910)	(1,910)

The above described changes had an effect of EUR -1,910 thousand on the income statement of the previous year; it pertains to a decrease in other operating revenue.

Reclassification of some received rebates and compensations

In order to achieve comparability with the year 2012, some received rebates and compensations in the amount of EUR 57,462 thousand were reclassified in the income statement for the year 2011; these rebates and compensations are now in both years recognised under the costs of sales, while earlier they had been included under sales of services. This modification resulted from an exact analysis of contracts made with the suppliers of merchandise, and of the interdependence between their contents and the quantities supplied. In this way, the sales of services now only comprise services independent of the purchase of merchandise, while other rebates and compensations are included in the costs of sales or in the inventories, depending on the actual sales of merchandise.

The changes described above only affect the income statement of the previous year, in terms of a decrease in sales revenue and decrease in costs of sales by EUR 57,462 thousand.

(v) Overall effect of the changes in accounting policies and other adjustments to financial statements

Adjustments of balance sheet as at January 1, 2011:

EUR thousand	Inventories	Deferred tax assets	Revenue reserves	Non-controlling interests	Current tax liabilities
As at January 1, 2011, originally reported	**322,081**	**8,700**	**270,194**	**246**	**5,892**
Effect of change in accounting policy	(25,068)	2,974	(21,458)	(3)	(633)
As at January 1, 2011, restated	**297,013**	**11,674**	**248,736**	**243**	**5,259**

Adjustments to balance sheet as at December 31, 2011:

EUR thousand	Intangible assets	Inventories	Deferred tax assets	Deferred tax liabilities	Revenue reserves	Profit (loss) for the year	Non-controlling interests	Current tax liabilities	Current tax assets
As at December 31, 2011, originally reported	**47,623**	**335,249**	**9,837**	**49,830**	**285,768**	**7,983**	**224**	**507**	**3,934**
Effect of the change in accounting policy at January 1, 2011	–	(25,068)	2,974	–	(21,458)	–	(3)	(633)	–
Effect of the change in accounting policy in 2011	–	(240)	(37)	–	–	(275)	–	126	128
Effect of accounting error in 2011	(9,851)	–	–	(985)	–	(8,866)	–	–	–
Effect of change of value of business combination in 2011	(1,910)	–	–	–	–	(1,910)	–	–	–
As at December 31, 2011, restated	**35,862**	**309,941**	**12,774**	**48,845**	**264,310**	**(3,068)**	**221**	**–**	**4,062**

Adjustments to the income statement for 2011:

EUR thousand	Change in revenue	Change in other income	Change in cost of goods sold	Impairments of intangible assets	Change in deferred taxes	Change in tax expenses	Change in profit (loss) for the year
2011, originally reported	**2,928,433**	**26,064**	**2,170,189**	**6,761**	**(137)**	**8,538**	**23,540**
Effect of the change in accounting policy in 2011	–	–	240	–	–	35	(275)
Effect of accounting error in 2011	–	–	–	9,851	(985)	–	(8,866)
Effect of change of value of business combination in 2011	–	(1,910)	–	–	–	–	(1,910)
Effect of reclassification of some received rebates and compensations	(57,462)	–	(57,462)	–	–	–	–
Total effect of changes	**(57,462)**	**(1,910)**	**(57,222)**	**9,851**	**(985)**	**35**	**(11,051)**
2011, restated	**2,870,971**	**24,154**	**2,112,967**	**16,612**	**(1,122)**	**8,573**	**12,489**

3. Significant accounting policies

The accounting policies laid out below have been applied consistently to all periods presented in these consolidated financial statements, by all Group entities.

(a) Basis of consolidation

(i) Business combinations

Business combinations are accounted at acquisition method as at the day of the combination, which is the same as the day of acquisition or when the Group gains control. Control shall be deemed to mean the power to make decisions on financial and business policies of the company or a business entity in order to reap benefits from company activities. To assess whether the Group has control, the criteria of currently exercisable potential voting rights shall be considered.

With regard to acquisitions, the Group shall measure or evaluate the goodwill as at the day of acquisition, as follows:

- at fair value of the transferred acquisition price; plus
- recognized value of any non-controlling interest in the acquired company; plus
- fair value of existing shares in equity of the acquired company, if the business combination is carried out in several steps; minus
- net recognized value (usually fair value) of acquired assets and liabilities as at the day of the acquisition.

If the difference is negative, it shall be recognized as surplus (income) in the income statement.
The transferred acquisition prices shall not include amounts of settlements regarding previously existing relations. These amounts are normally recognized in the income statement.
Acquisition costs, except for costs related to issue of equity or debt instruments related to the business combination, shall be recognized as they are incurred.

Contingent liabilities regarding business combinations shall be recognized at fair value as at the day of acquisition. If a contingent liability is classified as equity, it does not have to be evaluated again; payment shall be recognized within equity. Subsequent changes to fair value of a contingent liability shall be recognized in the income statement.

(ii) Subsidiaries

Subsidiaries are entities controlled by the Group. Control is deemed to exist when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that are currently exercisable are taken into account. Financial statements of subsidiaries are included in the consolidated financial statements from the date such control is commenced until the date such control ceases. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Group.

(iii) Acquisition of non-controlling interests

Acquisitions of non-controlling interests shall be accounted as transactions of shareholders who operate as owners; therefore, goodwill shall not be recognized. Changes in non-controlling interest derived from transactions that do not include loss of control shall be based on proportionate share of the subsidiary's net assets.

(iv) Loss of control

After loss of control, the Group shall reverse the recognition of assets and liabilities of the subsidiary, non-controlling interest, and recognition of other components of equity that pertain to the subsidiary. Any gains or losses from loss of control shall be recognized in the income statement. If the Group retains a shareholding/interest in the previously controlled subsidiary, such share shall be valued at fair value as at the day of loss of control. Subsequently, such share shall be recognized in equity as investment into associate (at equity method) or as available-for-sale financial assets, depending on the extent of retained influence.

(v) Transactions eliminated on consolidation

Intra-group balances, income and expenses arising from intra- group transactions, are eliminated from the consolidated financial statements. Unrealized losses are eliminated in the same way as gains, but only to the extent that there is no evidence of impairment.

(b) Foreign currency

(i) Foreign currency transactions

Transactions in foreign currencies are translated to the respective functional currency of Group entities at exchange rates effective at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies as at the reporting date are re-translated to the functional currency at the exchange rate effective at that date. The foreign currency gain or loss on monetary items is the difference between amortized cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortized cost in foreign currency translated at the exchange rate at the end of the period. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are re-translated to the functional currency at the exchange rate effective at the date the fair value was determined. Currency translation differences shall be recognized in income statement, except for differences arising on re-translation of equity instruments classified ass available-for-sale financial assets (except for the case of impairment when all currency translation differences recognized in other comprehensive income shall be re-classified to income statement), for non-financial liabilities designated as hedges (if such hedges are effective), or for cash flow hedges (if such hedges are effective) which are recognized directly in equity.

(ii) Foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated to euro at exchange rates effective at the reporting date. The income and expenses of foreign operations, excluding foreign operations in hyperinflationary economies, are translated to euro at average exchange rates.

Currency translation differences arising from translation shall be recognized directly in other comprehensive income and they shall be recognized in translation reserve within equity. From the day of transition to the IFRS, these changes shall be recognized in the translation reserve. When a foreign operation is disposed of, in part or fully, the relevant amount in the currency translation reserve (FCTR) is transferred to profit or loss.

In case of a subsidiary that is not in total control, a pro rata share of currency translation reserve is allocated to non-controlling interest. When a company abroad (foreign operation) is disposed of in a way that it is no longer controlled and that significant influence or joint control no longer exist, corresponding accrued amount in the currency translation reserve shall be transferred to profit or loss, or re-classified as revenue or expense resulting from the disposal. If the Group which only disposes of a part of its stake in a subsidiary that includes a foreign company, and still maintains significant influence or common control, an appropriate pro rata share of accumulated amount is allocated to non-controlling interests.

(c) Financial instruments

(i) Non-derivative financial instruments

Non-derivative financial instruments comprise investments in equity and debt securities, trade and other receivables, cash and cash equivalents, loans and borrowings, and trade and other payables.

Initially, the Group recognizes loans and receivables and deposits on the day of their occurrence. Other financial assets (including assets which are estimated at their fair value through profit or loss) are initially recognized on an exchange date or when the Group becomes a client in accordance with contractual terms of the instrument.

The Group shall correct the recognized financial assets when the contractual rights to cash flows of such assets expire or when Group moves the rights to contractual cash flows of financial asset related to a business in which all risks and benefits from ownership of the financial asset are transferred. Any share in the transferred financial asset that is created or transferred by the Group shall be recognized as individual asset or liability.

Financial assets and liabilities shall be offset and the net amount shall be reported in the balance sheet, but only if the Group has a legal right to settle the net amount or to realize the asset and at the same time settle the liability.

Loans and receivables

Loans and receivables are financial assets with fixed payments, which are not listed in an active market. These assets are initially recognized at their fair value increased by related direct costs. Later, these assets are recognized at amortized cost using the effective interest method, decreased by losses or impairments. Loans and receivables include cash and cash equivalents, loans to other companies and bank deposits, trade and other receivables, and long-term deposits for rent payment. Long-term deposits for rent payment are considered in terms of content (finance lessors) and represent long-term financial receivables. They shall be discounted with market or contractual discount rates. Discount rate shall be the basis for accounting of finance income in the entire period for which the rent was paid (see Note 22).

Cash and cash equivalents
Cash and cash equivalents include cash in hand and call deposits.

Available-for-sale financial assets
Available-for-sale financial assets are those non-derivative financial assets that are designated as available for sale or are not classified into the above categories (see Note 17). Available-for-sale financial assets include investments into shares and interests of enterprises. After the initial recognition, these investments are measured by fair value, also taking into account the changes in fair value. Impairment losses (see Note 3(i)(i)) and foreign exchange differences on available-for-sale financial monetary items (see Note 3(c)(i)) are recognized in other comprehensive income and reported in equity or in fair value reserve. When an investment is de-recognized, the cumulative gain or loss is transferred to profit or loss. Available-for-sale financial assets also include equity securities.

(ii) Non-derivative financial liabilities

Initially, the Group recognizes issued debt securities and subordinate debt at the date of their occurrence. All other financial liabilities shall be initially recognized as at their trading date when the Group becomes the contractual client related to that instrument.

The Group eliminates the recognition of financial liability, if obligations determined in contract are met, repealed or obsolete.

Financial assets are offset and the amount is recognized in the balance sheet if the Group has the official enforceable right to offset recognized amounts and intent to pay net amount or it is legally entitled to offset amounts and has intent to pay net amount or realize the asset and on the same time settle the liability.

Group recognizes non-derivative financial instruments as other financial liabilities. These financial liabilities are initially recognized at their fair value increased by the directly related costs. Subsequently, these financial liabilities are measured at amortized cost using the effective interest method.

Other financial liabilities include loans and trade and other payables.

(iii) Share capital

Ordinary shares
Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares and share options are recognized as a deduction from equity, net of any tax effects.

Repurchase of share capital (treasury shares)
When share capital recognized as equity is repurchased, the amount of consideration paid, which includes directly attributable costs, is net of any tax effects, and is recognized as a deduction from equity. Repurchased shares are classified as treasury shares and are presented as a deduction from total equity. When treasury shares are sold or reissued subsequently, the amount received is recognized as an increase in equity, and the resulting surplus or deficit on the transaction is transferred to capital reserves or retained earnings.

(iv) Derivative financial instruments

The Group holds derivative financial instruments to hedge its foreign currency and interest rate risk exposures.

Upon the inception of the hedge, the Group shall keep formal documents about the ratio between risk management and the purpose of risk management at the company, and about the strategy of the hedge project, as well as the methods used in estimating the effectiveness of this ratio. The group estimates the hedge with conventional method and at its inception, when highly successful hedge is expected to reach the offset changes of fair value or cash flows which are added to hedge, and when the realized amounts reach 80 - 125 percent. With cash flow hedges, the expected business/transaction that is the subject of hedging must be highly probable and exposed to cash flow changes which could ultimately affect the profit or loss in a decisive manner.

Derivatives are initially recognized at fair value; attributable transaction costs are recognized in profit or loss when incurred. Subsequently to initial recognition, derivatives shall be measured at fair value, and changes therein shall be accounted for as described below.

Cash flow hedges
When a derivative financial instrument is classified as a cash flow hedge, hedging from exposure to the changes in cash flow attributable to an individual type of risk related to a recognised asset or liability, or highly probable announced or anticipated transactions which may affect profit or loss, then the effective (successful) part of changes in the fair value of the derivative financial instrument shall be recognized in other comprehensive income for the period, and disclosed in the hedging reserve or equity item. Ineffective (unsuccessful) part of the changes to the fair value of the derivative financial instruments shall be recognized directly in profit or loss.

If the hedged item is a non-financial asset, the amount shall be transferred to the carrying (book) value of such asset upon recognition. In other cases, the amount recognized through equity shall be transferred to the income statement for the period in which the hedged item affects the profit or loss. As a rule, a hedge shall no longer be accounted for or recognized by the Group if a hedging instrument no longer meets the criteria for hedge accounting, if it is disposed, waived, or exercised/called, or if the company cancels the designation. If the anticipated transaction is no longer probable, the amount in other comprehensive income shall be recognized directly in profit or loss (income statement).

(d) Property, plant, and equipment

(i) Reporting and measurement
Plant and equipment are measured using the cost model. They are carried at their cost less any accumulated depreciation and any accumulated impairment losses.

Cost includes expenditure that is directly attributable to the acquisition of the asset. Lease costs pertaining to acquisition or construction of relevant property, plant, or equipment, shall be capitalized if they are related to the acquisition of a major asset and if construction or preparation for use lasts over 6 months. In 2012 the group has not made capital expenditures, which would meet the described criteria. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use, and the costs of dismantling and removing the items and restoring the site on which they are located, as well as capitalized borrowing costs.

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal of an item of property, plant and equipment with the net value (carrying amount) recognized in other income/expenses in the income statement. When revalued assets are sold, the amounts included in the revaluation surplus reserve are transferred to retained earnings.

The Group employs the revaluation model to measure the value of land and buildings. The fair values reported are based on periodical, but not less than three-year valuations by an external independent appraiser, less accumulated depreciation. Fair value of real estate shall be estimated or appraised in compliance with the International Valuation Standards (IVS 2011) and Slovenian business and financial standard No. 2 – valuation/appraisal of real estate (OJ RS 56/2001). To appraise the market value, the possibilities and suitability of all three methods shall always be examined considering the type of property, its use, and availability of information. These three methods include capitalization of gain (discounted cash flow method); comparable sales (method of direct comparability of sales or transactions), and historical cost (historical cost method). In valuation of land, the method of comparable sales and method of residual value. In valuation of buildings, the value shall be considered, which was calculated either with the method of comparable sales (real estate that is a part of a building, for which an active real estate market exists) or historical cost method (individual buildings constructed for a specific purpose – trade centers). If the book/carrying value of an asset is increased as a result of revaluation, the increase shall be recognized directly in equity as revaluation surplus. The increase shall be recognized in profit or loss (income statement) if it eliminates a revaluation decrease of the same asset, which had previously been recognized in profit or loss. If the book/carrying value of assets is decreased as a result of revaluation, then the decrease shall be recognized in profit or loss. Decrease shall be charged directly to equity under the item revaluation surplus, up to the amount of credit in the revaluation surplus for the same asset. When an asset is divested or disposed of, or when its value is decreases as a result of depreciation and amortisation, the fair value reserve for such asset shall be transferred directly to retained earnings.

Depreciation charge based on revalued value of assets shall be recognized in the income statement. Useful life and remaining value of buildings shall be evaluated/appraised by an internal committee of experts in case of events that indicate the need for revaluation of a particular asset.

a) Estimation of fair value of real property

In compliance with the Accounting Rules, the Group periodically, at least three times per year, reviews the fair values of its real estate. Real estate valuation was made on October 31, 2012 by a certified real estate appraiser in accordance with the International Valuation Standards and International Financial Reporting Standards.

Pursuant to the International Accounting Standards, the Group defined already in 2005 its cash-generating units for the purposes of determining the fair value of real property. One such unit shall include all real estate located at same location/address.

The revaluation effect in 2012 is positive and it amounts to a total of EUR 20,402 thousand.

EUR thousand	Fair value reserve	Profit (loss) for the year	Total
value increases	73,570	–	73,570
reversal of value increases	(18,425)	–	(18,425)
impairments	–	(35,118)	(35,118)
reversal of impairments	–	375	375
Total effect on value of real estate	**55,145**	**(34,743)**	**20,402**

b) Assessment of useful lives of property, plant and equipment

At Mercator Group, property, plant and equipment are depreciated by the straight line depreciation method, using the depreciation rates that reflect estimated useful lives of different assets at each Mercator Group company. Useful lives and residual value of property, plant and equipment shall be tested annually by internal experts or external independent appraisers based on any events that indicate the need for revaluation of a particular asset.

(ii) Reclassification to investment property

If a piece of real estate used by the owner is transformed into investment property, such property shall be evaluated by its historical cost with elimination of fair value reserve; then, it shall be transferred to investment property. The Group evaluates its investment property by the cost model. Only independent real estate units entirely leased to a third party shall be classified as investment property. If only a part of a building/facility is leased to a third party, it is not classified as investment property, as it cannot be sold separately, and because the other important part of the facility is being used for selling or producing goods.

(iii) Subsequent expenditure

The cost of replacing a part of a piece of property, plant and equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within that part will flow to the Group and its cost can be measured reliably. The carrying amount of the replaced part shall be de-recognized. The costs of the day-to-day servicing of property, plant and equipment shall be recognized in profit or loss as soon as they are incurred.

(iv) Depreciation

Depreciation is calculated on a straight-line basis over the estimated useful lives of respective parts of an item of property, plant and equipment. Leased assets are depreciated by taking into account the lease term and their useful lives, unless it is reasonably certain that the company will obtain ownership by the end of the lease term. Land is not depreciated.

For the part of the depreciation that relates to revalued property, plant, and equipment, the Group shall continuously eliminate the established revaluation surplus in retained earnings.

The estimated useful lives for the current and comparative periods are as follows:

	2012	2011
Buildings	20-50 years	20-50 years
Plant and equipment	2-18 years	2-18 years

Useful lives and residual values are reviewed at each reporting date.

(e) Intangible assets

(i) Goodwill

Goodwill generated upon acquisition of subsidiaries shall be recognized as intangible asset (see also 3 (a)(i)).

(ii) Other intangible assets

Other intangible assets that are acquired by the Group, which have finite useful lives, are measured at cost less accumulated amortization and accumulated impairment losses.

(iii) Subsequent expenditure

Subsequent expenditure is capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure, including internally generated brands, shall be recognized in profit or loss as soon as they are incurred.

(iv) Amortization

Amortization is calculated on a straight-line basis over the estimated useful lives of intangible assets (except for goodwill which is tested for impairment annually). It shall be recognized from the date the intangible asset is available for use. The estimated useful lives for the current and comparative periods are as follows:

	2012	2011
Brands/labels	10 years	10 years
Software and licenses	5-10 years	5-10 years

(f) Investment property

Investment property is property held either to earn rental income or for capital appreciation or for both, but not for sale in the ordinary course of business, use in the production or supply of goods or services, or for administrative purposes.

Only independent real estate units that are entirely leased to third parties are classified as investment property. If only a part of property (building) is leased out, it shall not be transferred to investment property as it cannot be sold separately and since other relevant part of the building is used for performance of in-house service activity or production of goods (e.g. a hypermarket within a shopping center). Investment property is recorded by the cost model. Depreciation is calculated based on a linear method, so that the purchase value of assets is divided on their respective remaining values throughout the anticipated useful life which shall be deemed to be 30 to 33 years for the current and comparable year.

When the use of property changes so that it is reclassified as property, plant and equipment, the fair value of such asset shall be measured. Positive difference shall be recognized in fair value reserve, while negative difference shall be recognized in the income statement.

(g) Leased assets

Leases in terms of which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition, the leased asset shall be reported at an amount equal to the lower of either fair value or the present value of the sum of minimum lease payments. Subsequently to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases shall be considered operating leases. Assets in operating lease shall not be reported in the Group's balance sheet.

(h) Inventories

Inventories are measured at the lower of cost and net realizable value.

Inventory valuation methods:

- retail price method including profit margin and VAT in retail,
- wholesale price method including profit margin in wholesale,
- historical cost method for raw and processed material.

Following are the methods of calculating the cost of inventories and relevant expenses:

- FIFO method for merchandise,
- method of average purchase prices (cost) for raw materials and packaging; cost of inventory includes purchase value, cost of production, transformation, and other costs incurred in bringing them to the current location and in the current condition; with both finished products and semi-products, the costs also include the relevant part of indirect production cost, under the assumption of normal use of means of production.

The net realizable value is equal to the estimated selling price in the ordinary course of business, less

the estimated costs of completion and the estimated costs necessary to make the sale.
The estimation of net realizable value of inventory is conducted at least once per year, upon the compilation of regular annual inventory lists.

Write-offs and partial write-offs of damaged, expired, and dead inventories shall be conducted regularly during the year on specific items. At the end of the year, inventories shall be impaired as at December 31 by groups of related or connected items depending on their ageing or obsoleteness. They are impaired on the basis of previous years' experience.

(i) Impairment of assets

(i) Non-derivative financial assets

For each financial asset that is not recognized at its fair value through profit or loss, an assessment is made on the reporting date to determine whether there is objective evidence from which the impairment of an asset is seen. Financial asset is impaired if there is objective evidence indicating that after the initial recognition of asset, there was, for one ore a number of events, a decrease of expected cash flows from this asset and this difference in cash flows can be measured.

Objective evidence that financial assets (including equity securities) are impaired can include default or delinquency by a debtor, restructuring of an amount owed to the Group subject to Group's consent; indications that bankruptcy proceedings will be instituted for a debtor; adverse changes in the payment ability of borrowers or issuers in the Group; and economic conditions that correlate with the disappearance of an active market for a security. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment. The Group's equity securities shall be impaired if the stock market price of a security is continuously below the security's acquisition price for at least 6 months, or if the current stock market price of the investment is more than 20% lower than its acquisition price.

Loans and receivables

The Group shall consider any evidence of impairment for loans and receivables at both specific asset and collective (grouped) level. All significant receivables shall be assessed individually for specific impairment. All individually significant loans and receivables found not to be specifically impaired shall be collectively assessed for any impairment that has been incurred but not yet identified. Loans and receivables that are not individually significant are collectively assessed for impairment by grouping together loans and receivables with similar risk characteristics.

In assessing collective impairment the Group uses historical trends of the probability of default, the timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical trends.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses shall be recognized in profit or loss and disclosed in an allowance account against loans and receivables. Interest on the impaired asset continues to be recognized. When a subsequent event (e.g. repayment by a debtor) causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

Available-for-sale financial assets

Impairment losses on available-for-sale financial assets shall be recognized by transferring the losses accumulated in the fair value reserve in equity, to profit or loss. The cumulative loss that is reclassified from equity to profit or loss is the difference between the acquisition cost and the current fair value, less any impairment loss recognized previously in profit or loss.

If, in a subsequent period, the fair value of an impaired available-for-sale equity security increases and the increase can be related objectively to an event occurring after the impairment loss was recognized in profit or loss, then the impairment loss cannot be reversed trough profit or loss. Any subsequent recovery in the fair value of an impaired available-for-sale equity security is recognized in other comprehensive income.

(ii) Non-financial assets

The carrying amounts of the Group's non-financial assets, other than investment property, inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. For goodwill and intangible assets that have indefinite lives or that are not yet available for use, the recoverable amount is estimated on each reporting date. Impairment of cash-generating unit is recognized when its carrying amount exceeds its recoverable amount.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets, which cannot be tested separately, are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit" or CGU). Subject to an operating segment ceiling test, for the purposes of goodwill impairment testing, CGUs to which goodwill has been allocated shall be aggregated so that the level at which impairment testing is performed reflects the lowest level at which goodwill is monitored for internal reporting purposes. The goodwill acquired in a business combination, for the purpose of impairment testing, shall be allocated to cash-generating units or groups of units that are expected to benefit from synergies of the combination.

The Group's corporate assets do not generate separate cash inflows and are utilized by more than one CGU. Corporate assets shall be allocated to CGUs on a reasonable and consistent basis. They shall be tested for impairment as part of the testing of the CGU to which the corporate asset is allocated.

An impairment loss is recognized in income statement. Impairment losses recognized in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. In respect of other assets, impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

(j) Employee benefits

(i) Other long-term employee benefits – retirement benefits and jubilee premium provisions

In the balance sheet, the Group recognized long-term provisions deriving from future liabilities to employees for long service awards, calculated in compliance with the collective labour agreement for this industry, and the mandatory retirement benefits as stipulated by the relevant act. The changes in retirement benefits and jubilee premiums provisions are recognized in the income statement. The provisions are determined based on actuarial calculations that are revised annually. Actuarial gains or losses are the effect of changed facts that affect the actuarial calculation (e.g. change in legislation), or a change in actuarial assumptions.

The calculation shall be prepared by considering the cost of retirement benefit for each employee, considering the collective labour agreement, and the cost of all expected jubilee premiums for employees with permanent employment contracts, as at December 31, 2012. The calculations also include actually enacted provisions regarding retirement terms and conditions, expected increase in salaries in the industry, estimate employee fluctuation, and a suitable discount rate that allows calculating the present value of all future expected payments of retirement benefits and jubilee premiums. All parameters are adjusted to the specific aspects of legislation in individual countries in which legal entities of the Mercator Group are located.

(ii) Termination benefits

Termination benefits are recognized as an expense when the Group is committed demonstrably, without realistic possibility of withdrawal, to a formal detailed plan to either terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits for voluntary redundancies are recognized as an expense if the Group has made an offer of voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably.

If benefits are payable more than 12 months after the reporting date, then they are discounted to their present value.

(iii) Short-term employee benefits
Short-term employee benefit obligations shall be measured on a non-discounted basis; they shall be expensed as the related service is provided.

A liability is recognized for the amount expected to be paid under short-term cash bonus if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(k) Provisions

A provision is recognized if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax discount rate that reflects current market assessments of the time value of money and, if required, the risks specific to the liability.

(i) Onerous contracts
A provision for onerous contracts is recognized when the expected benefits to be derived by the Group from a contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract. Before a provision is established, the Group recognizes any impairment loss on the assets associated with that contract.

(ii) Restructuring
A provision for restructuring is recognized when the Group has approved a detailed and formal restructuring plan, and the restructuring either has commenced or has been announced publicly. Future operating losses are not provided for.

(l) Revenue

(i) Revenue from sales of goods, products, and material
Revenue from the sale of goods, products and material is measured at the fair value of consideration received or receivable, net of returns, trade discounts and volume rebates. Revenue is recognized when the significant risks and rewards of ownership have been transferred to the buyer, recovery of consideration is probable, the associated costs and possible return of goods, products and material can be estimated reliably, there is no continuing management involvement with the quantity of goods sold, and the amount of revenue can be measured reliably.

Transfers of risks and rewards vary depending on the individual terms of the contract of sale. For wholesale of goods, transfer usually occurs when the product is received at the customer's warehouse; however, for some international shipments transfer occurs upon loading the goods onto the relevant carrier.

(ii) Customer loyalty program
The Group issues credit and debit cards Mercator Pika to its customers for collecting bonus points at purchases. Bonus periods last six months. The first bonus period in the year lasts from February 1 to July 31 the second bonus period from August 1 to January 31 of the following year. During the bonus period, customers collect bonus points. Depending on the amount of purchases and consequently the number of collected points, they can earn a 3 to 6-percent discount. During the year, the Group shall allocate potential discounts on the basis of collected points, whereas revenue from unrealized bonus points is allocated based on experience from previous bonus periods. Despite the fact that the second bonus period ends on January 31 the following year, the Group in this way ensures that recorded revenues match expenditures that were necessary for their realization.

(iii) Revenue from services rendered
Revenue from services rendered is recognized in profit or loss in proportion to the stage of completion of the transaction at the reporting date. The stage of completion is assessed by reference to surveys of work performed.

(iv) Rental income
Rental income is recognized in profit or loss on a straight-line basis over the term of the lease. Any discounts and benefits granted are recognized as an integral part of the total rental income.

(m) Government grants

All types of government grants are recognized initially as deferred income when there is reasonable assurance that they will be received and that the Group will comply with the conditions associated with the grant. Grants that compensate the Group for expenses incurred are recognized in profit or loss on a systematic basis in the same periods in which the expenses are recognized. Grants that compensate the Group for the cost of an asset are recognized in profit or loss among other income on a systematic basis over the useful life of the asset.

(n) Leases

Payments made under operating leases are recognized in profit or loss on a straight-line basis over the term of the lease. Lease discounts and benefits received are recognized as an integral part of the total lease expense.
Payments made under financial leases are recognized in profit or loss on a straight-line basis over the term of the lease. Lease discounts and benefits received are recognized as an integral part of the total lease expense.

Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

Determining whether an arrangement includes a lease
At inception of an arrangement, the Group determines whether such an arrangement is or contains a lease. This shall be deemed to be the case if the following criteria are met:

- a specific asset shall be deemed the subject of a lease if the fulfilment of the arrangement is dependent on the use of that specified asset; and
- if an arrangement conveys the right to use the asset.

At inception or upon reassessment of the arrangement, the Group separates payments and other consideration required by such an arrangement into those for the lease and those for other elements on the basis of their relative fair values. If the Group concludes for a finance lease that it is impracticable to separate the payments reliably, then an asset and a liability are recognized at an amount equal to the fair value of the underlying asset. Subsequently the liability is reduced as payments are made and an imputed finance charge on the liability is recognized using the Group's incremental borrowing rate.

(o) Finance income and expenses

Finance income comprises interest income on funds invested (including available-for-sale financial assets), dividend income, gains on the disposal of available-for-sale financial assets, changes in the fair value of financial assets at fair value through profit or loss, gains on revaluation of fair value of interest in an acquired company that the Group had held in the acquired company before the acquisition, and gains on hedging instruments that are recognized in profit or loss. Interest income is recognized as it accrues, using the effective interest method. Dividend income shall be recognized in the income statement as at the day when the shareholder's right to payment is asserted; for companies listed on the stock market, this is, as a rule, the day when the right to current dividend ceases to be related to the share.

Finance expenses comprise interest expense on borrowings, unwinding of the discount on provisions and contingencies, impairment losses recognized upon disposal of available-for-sale financial assets, dividend on preferred stock reported in liabilities, negative changes/impairments to the fair value of financial assets at fair value through profit or loss, losses on hedging instruments that are recognized in profit or loss, and reclassification of amounts previously recognized as other comprehensive income.
Borrowing costs that do not pertain directly to acquisition, construction, or production of an asset under construction shall be recognized in the income statement according to effective interest method.

Gains and losses from translation between currencies shall be recognized at net value as finance income or finance expenses.

(p) Corporate income tax

Income tax expense for the year comprises current and deferred tax. Income tax expense shall be recognized in profit or loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity or other comprehensive income.

(i) Current tax expense
Current tax is the expected tax payable on the taxable income for the year, using tax rates

enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

(ii) Deferred tax

Deferred tax is recognized using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized for the following temporary differences:

- the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit,
- differences relating to investments in subsidiaries and jointly controlled entities to the extent that it is probable that they will not reverse in the foreseeable future,
- taxable temporary differences upon initial recognition of goodwill.

Deferred tax liabilities are measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted at the reporting date.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilized. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

(q) Net earnings per share

The Group calculates basic earnings per share by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period. Since the Group does not have any preference shares or convertible bonds, diluted earnings per share are the same as basic earnings per share.

4. New standards and interpretations not yet adopted

The following new standards and interpretations have not yet been adopted and they were not considered in development of financial statements as at December 31, 2012.

- *Amendment to IFRS 7 Disclosures – Offsetting Financial Assets and Financial Liabilities* (Effective for annual accounting periods starting on January 1, 2013, and interim periods within these accounting periods. Use before this date is also allowed.)

- *IFRS 10 Consolidated Financial Statements and IAS 27 (2011) Separate Financial Statements* (Effective for annual accounting periods starting on January 1, 2014; use before this date is only allowed in case of early use of IFRS 11, IFRS 12, IAS 27 (2011), and IAS 28 (2011).) The standard shall be applied retroactively, if there are changes in the findings regarding control.

- *IFRS 11 Joint Arrangements* (Effective for annual accounting periods starting on January 1, 2014; to be used retroactively subject to transitory provisions. Use before this date shall only be allowed in case of early use of IFRS 10, IFRS 12, IAS 27 (2011) and IAS 28 (2011).)

- *IFRS 12 Disclosure of Interests in Other Entities* (Effective for annual accounting periods starting on January 1, 2014; to be used retroactively subject to transitory provisions. Use before this date is also allowed.)

- *IFRS 13 Fair Value Measurement* (Effective for annual accounting periods starting on January 1, 2013; it is to be used henceforth. Use before this date is also allowed.)

- *Amendment to IAS 1 Presentation of Financial Statements: Presentation of Other Comprehensive Income* (Effective for annual accounting periods starting on July 1, 2012; it is to be used retroactively. Use before this date is also allowed.)

- *Amendment to IAS 12: Corporate income tax: Recovery of Underlying Assets* (Effective for annual accounting periods starting on January 1, 2013; it is to be used retroactively. Use before this date is also allowed.)

- *IAS 19 (2011) Employee Benefits* (Effective for annual accounting periods starting on January 1, 2013; it is to be used retroactively. Transitory provisions apply. Use before this date is also allowed.)

- *IAS 28 (2011) Investments in Associates and Joint Ventures* (Amendments effective for annual accounting periods starting on January 1, 2014; to be used retroactively. Use before this date shall only be allowed in case of early use of IFRS 10, IFRS 11, IFRS 12, and IAS 27 (2011).)

- *Amendment to IAS 32 – Offsetting Financial Assets and Financial Liabilities* (Effective for annual accounting periods starting on January 1, 2014; to be used retroactively. Use before this date shall be allowed subject to disclosures pursuant to amendment to IFRS 7 Disclosures – Offsetting Financial Assets and Financial Liabilities.)

- *IFRIC 20 Stripping Costs in the Production Phase of a Surface Mine* (Effective for accounting periods starting on January 1, 2013; to be used henceforth for stripping costs incurred after the start of the earliest presentation period. Use before this date is also allowed.)

In our estimate, only the amendment to IAS 1 – Presentation of Financial Statements: Presentation of Other Comprehensive Income shall affect the financial statements of Mercator Group in the future. This amendment requires:

- that the company present separately the items of other comprehensive income which may be transferred/re-classified in the future to profit or loss, and those that will never be re-classified to profit or loss; if the items of other comprehensive income are presented before related tax effects, then the entire amount of tax shall also be presented or classified within these sections;
- a change of the title "Statement of Comprehensive Income" to "Statement of Profit or Loss and Other Comprehensive Income", although other titles shall also be allowed.

5. Determination of fair values

A number of the Group's accounting policies and disclosures require the determination of fair value for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and / or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

(a) Property, plant, and equipment

Fair value of property, plant and equipment from business combinations shall be equal to their market value at which a willing buyer and a willing seller would trade the property as at the day of the appraisal of value in a transaction between non-associated and independent parties after reasonable marketing, with both parties taking part in the trade being informed, prudent, and without force or coercion. Description of the determination of the fair value of real estate is included in Note 3 (d) Property, plant, and equipment.

(b) Intangible assets

The fair value of patents and trademarks acquired in a business combination is based on the discounted estimated royalty payments that have been avoided as a result of the patent or trademark being owned. The fair value of other intangible assets is based on the discounted cash flows expected to be derived from the use and eventual sale of the assets.

(c) Investment property

The fair values in business or strategic combinations are based on market values, being the estimated amount for which a property could be exchanged on the date of the valuation between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion (arm's length transaction).

In the absence of current prices in an active market, the valuations are prepared by considering the aggregate of the estimated cash flows expected to be received from renting out the property. A yield that reflects the specific risks inherent in the net cash flows then is applied to

the net annual cash flows to arrive at the property valuation.
Valuations reflect, when appropriate: the type of tenants actually in occupation or responsible for meeting lease commitments or likely to be in occupation after letting vacant accommodation, and the market's general perception of their creditworthiness; the allocation of maintenance and insurance responsibilities between the Group and the lessee; and the remaining economic life of the property. When rent reviews or lease renewals are pending with anticipated reversionary increases, it is assumed that all notices, and when appropriate counter-notices, have been served validly and within the appropriate time.

(d) Inventories

The fair value of inventories acquired in business combinations shall be determined based on their estimated selling price in the ordinary course of business, less the estimated costs of completion and sale, and a reasonable profit margin considering the effort required to complete and sell the inventories.

(e) Investments in equity and debt securities

The fair value of financial assets at fair value through profit or loss, held-to-maturity investments and available-for-sale financial assets in business or strategic combinations is determined by reference to their quoted bid price at the reporting date, or if not available, determined using a valuation technique. Valuation techniques which can be employed include market multiples and discounted cash flow analysis using expected future cash flows and a market-related discount rate. The fair value of held-to- maturity investments is determined for disclosure purposes only.

(f) Trade and other receivables

The fair value of trade and other receivables, excluding construction work in progress, in business or strategic combinations is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date.

(g) Derivatives

The fair value of forward exchange contracts is based on their listed market price, if available. If a listed market price is not available, then fair value is estimated by discounting the difference between the contractual forward price and the current forward price for the residual maturity of the contract using a risk-free interest rate (based on government bonds).

The fair value of interest rate swaps is based on broker quotes. Those quotes are tested for reasonableness by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates for a similar instrument at the measurement date.

(h) Non-derivative financial liabilities

Fair value, which is determined for disclosure purposes, is calculated based on the most recent market value of bonds in the stock market, prior to the reporting date. Fair values of other non-derivative financial liabilities are not determined, as the carrying amount represents a reasonable approximation of fair value.

6. Tax policy

(a) Slovenia

Tax statements (financial statements for tax authorities) of the company Poslovni sistem Mercator, d.d., and the companies of the Mercator Group in Slovenia, are prepared in accordance with International Financial Reporting Standards and the Corporate Income Tax Act.

In 2012, changes were made to the provisions of the Corporate Income Tax Act, which affected the tax statements of the Mercator Group companies in Slovenia. The tax rate was decreased to 18%; absolute cap to the relief for investment into equipment and intangible non-current assets in the amount of 40% of the invested amount no longer applies.

Pursuant to the corporate Income Tax Act, a company's taxable base is the profit as the surplus of revenues over expenses, where the basic criteria for recognition, or inclusion, in a tax statement are still the revenues and expenses as shown in the income statement, defined pursuant to the legislation or accounting standards.

Pursuant to IAS 12, the Mercator Group companies in Slovenia re-calculated their deferred income tax as at December 31, 2012, at the rate of 17%, which shall be used for corporate income tax as of January 1, 2013. In 2012, the companies recognized and reversed deferred income tax related to the following items:

- differences between business and tax recognized depreciation,
- impairment of receivables,
- provisions made,
- tax losses;
- revaluation of goodwill;
- change in fair value of derivative financial instruments,
- revaluation of property, plant and equipment,
- property, plant and equipment, whose value does not exceed EUR 500 and whose useful life is longer than one year,
- change in fair value of available-for-sale financial assets;
- revaluation of investment into equity of subsidiaries.

Each company shall provide documentation on transfer prices; general documentation may be common to a group of related entities as a whole.

(b) Serbia

Tax statements of the companies Mercator-S, d.o.o., Intersport S-ISI, d.o.o., and Modiana, d.o.o., Serbia, are prepared in compliance with International Financial Reporting Standards and the relevant Corporate Income Tax Act ("Zakon o porezu na dobit pravnih lica").

Corporate income tax rate is at 10 %.

In the assessment of corporate income tax, the following tax reliefs can be exercised:

- investment relief in the amount of 20% of the sum invested in the current year (but not more than 50% of levied tax).

As the tax rate is to be increased to 15% as of January 1, 2013, deferred income tax of the companies were adjusted as at December 31, 2012, pursuant to IAS 12, by applying the new rate. In 2012, Mercator Group companies in Serbia recognized and de-recognized deferred taxes related to the following items:

- differences between business and tax recognized depreciation,
- impairment of inventory,
- provisions made,
- revaluation (increase in value) of property, plant and equipment.

(c) Croatia

Tax statements of the companies Mercator-H, d.o.o., Intersport H, d.o.o., and Modiana, d.o.o., Croatia, are prepared in compliance with International Financial Reporting Standards and the relevant Corporate Income Tax Act ("Zakon o porezu na dobit").

Taxable base is the profit calculated according to the accounting principles, from which tax recognized costs are subtracted, or to which non-recognized costs are added. The company may also decrease its taxable base by the amount of revenues from dividends or participation in profit of other companies, and by depreciation that was not recognized as expense in previous periods.

Corporate income tax rate is at 20%.

In the assessment of corporate income tax, the following tax reliefs can be exercised:

- investment relief for promoting investments (under terms stated in the relevant act);
- investment relief for taxpayers in areas under special government protection.

In 2012, Mercator Group companies in Croatia recognized and de-recognized deferred taxes related to the following items:

- impairment of inventory,
- impairment of receivables,
- revaluation (increase in value) of property, plant and equipment.

(d) Bosnia and Herzegovina

Tax statements of the companies Mercator - BH, d.o.o., M - BL, d.o.o., Intersport BH, d.o.o., Modiana, d.o.o., Bosnia and Herzegovina, are prepared in compliance with International Financial Reporting Standards and the relevant Corporate Income Tax Act ("Zakon o porezu na dobit").

Corporate income tax rate is at 10 %.

In the assessment of corporate income tax, companies in Bosnia and Herzegovina may exercise the following tax reliefs:

- investment relief for investments in production on the territory of Bosnia and Herzegovina (taxpayers investing no less than BAM 20 million for 5 years in succession);
- investment relief for exports;

- investment relief for hiring disabled persons.

In 2012, Mercator Group companies in Bosnia and Herzegovina recognized and de-recognized deferred taxes related to differences between business and tax deductible depreciation.

(e) Montenegro

Tax statements of the company Mercator-CG, d.o.o., are prepared in compliance with International Financial Reporting Standards and the relevant Corporate Income Tax Act ("Porez na dobit pravnih lica").

Corporate income tax rate is at 9%.

In the assessment of corporate income tax, the following tax reliefs can be exercised:

- investment relief for newly hired, that are employed for indefinite time period, in the amount of their wages;
- investment relief for the acquisition of assets that increase energy efficiency (taxable base is decreased for 50% of completed investments).

In 2012, the company Mercator-CG, d.o.o., recognized deferred income tax assets due to differences between business and tax deductible depreciation.

(f) Bulgaria

Tax statements of the company Mercator-B, e.o.o.d., are prepared in compliance with International Financial Reporting Standards and the relevant corporate income tax ("Law on Corporate Income Taxation").

Corporate income tax rate is at 10%.

In the assessment of corporate income tax, the following tax reliefs can be exercised:

- investment relief for hiring handicapped persons;
- investment relief for taxpayers in areas, which are less developed (under terms stated in the relevant act);
- investment relief for newly hired employees (under terms stated in the relevant act).

In 2012, the company Mercator-B, e.o.o.d., recognized deferred income tax assets due to differences between business and tax deductible depreciation.

(g) Albania

Tax statements of the company Mercator-A, sh.p.k., are prepared in compliance with International Financial Reporting Standards and the Corporate Tax on Income.

Corporate income tax rate is at 20%.

In 2012, the company Mercator - A, sh.p.k., did not recognize deferred tax assets or liabilities.

7. Business segments

For the requirements of reporting by business segments, Mercator Group defined in 2012 the geographical segments consistently with the countries in which the Group is performing its activities. In our view, such presentation provides the users of financial statements with more accurate information, allowing them to more easily understand past achievements, and evaluate and consider the risks and returns of particular companies and the Group as a whole.

Mercator Group is active in seven countries:

- Slovenia, the location of the parent company, which is also the largest business unit of the Group. Fields of operation in Slovenia include the following: trade (retail and wholesale); food processing, and other non-trade activities;
- Serbia, Croatia, Bosnia and Herzegovina, Montenegro, Bulgaria, Albania. Operations in these countries are carried out in the business segment of trade.

Market prices are used for selling goods, products and services between the segments.

	Slovenia		Serbia		Croatia		Bosnia and Herzegovina		Montenegro		Bulgaria		Albania		Total	
EUR thousand	**2012**	**2011**	**2012**	**2011**	**2012**	**2011**	**2012**	**2011**	**2012**	**2011**	**2012**	**2011**	**2012**	**2011**	**2012**	**2011**
Total segment revenues	**1,644,530**	**1,688,240**	**561,000**	**553,262**	**382,366**	**412,191**	**194,230**	**131,131**	**104,915**	**100,712**	**9,310**	**8,536**	**4,298**	**5,445**	**2,900,649**	**2,899,517**
Inter-segment revenues	26,063	27,093	113	0	937	643	177	611	129	68	41	53	3	78	27,463	28,546
Depreciation and amortisation	(43,873)	(42,062)	(13,447)	(15,091)	(16,149)	(16,083)	(5,059)	(4,555)	(1,658)	(1,623)	(945)	(1,124)	(659)	(768)	(81,789)	(81,306)
Impairment of property, plant and equipment and intagible assets	(12,164)	(1,850)	(854)	(10,464)	(36,971)	(3,178)	(1,235)	(21)	-	(5)	(5,207)	(919)	(3,411)	-	(59,842)	(16,438)
Total segment results from operating activities	**25,352**	**77,532**	**12,666**	**13,682**	**(55,449)**	**(8,294)**	**(300)**	**2,854**	**(25)**	**57**	**(17,616)**	**(6,608)**	**(6,776)**	**(2,383)**	**(42,147)**	**76,841**
Interest income	4,002	4,350	534	382	175	173	1,441	302	587	178	1	12	-	-	6,740	5,398
Interest expense	(36,464)	(38,843)	(4,634)	(4,430)	(9,145)	(9,514)	(2,354)	(1,673)	(437)	(50)	(913)	(704)	(359)	(416)	(54,305)	(55,630)
Income tax	6,294	(7,206)	(804)	(80)	421	(36)	(204)	(172)	(69)	64	21	(21)	-	-	5,659	(7,451)
Assets	1,474,056	1,468,404	435,265	449,635	471,322	534,893	167,958	137,124	58,894	49,359	5,708	13,205	2,177	7,572	2,615,379	2,660,193
Liabilities	1,214,690	1,245,699	265,937	237,547	313,136	318,853	94,516	61,758	26,465	16,045	27,790	16,776	9,596	7,058	1,952,130	1,903,736
Capital expenditure	42,563	36,053	17,829	51,293	2,373	17,820	3,369	4,053	974	5,569	212	889	10	147	67,330	115,824

Reconciliation of reportable segment revenues, results from operating activities, assets and liabilities, and other material items

Revenue

EUR thousand	2012	2011
Total segment revenue	2,900,649	2,899,517
Elimination of inter-segment revenue	(27,463)	(28,546)
Consolidated revenue	**2,873,186**	**2,870,971**

Results from operating activities

EUR thousand	2012	2011
Total reportable segment results from operating activities	(42,147)	76,841
Elimination of inter-segment profits	–	–
Consolidated results from operating activities	**(42,147)**	**76,841**

Assets

EUR thousand	2012	2011
Total assets for reportable segments	2,615,379	2,660,193
Inter-segment elimination	(92,559)	(46,534)
Consolidated total assets	**2,522,820**	**2,613,659**

Liabilities

EUR thousand	2012	2011
Total liabilities for reportable segments	1,952,130	1,903,736
Inter-segment elimination	(92,559)	(46,534)
Consolidated total liabilities	**1,859,571**	**1,857,202**

Other material items 2012

EUR thousand	Reportable segment totals	Inter-segment eliminations	Consoli-dated totals
Interest income	6,740	(3,366)	3,374
Interest expense	(54,305)	3,366	(50,939)
Depreciation and amortization	(81,789)	–	(81,789)
Impairment of property, equipment, and intangible assets	(59,842)	–	(59,842)
Income tax	5,659	–	5,659
Capital expenditure	67,330	–	67,330

Other material items 2011

EUR thousand	Reportable segment totals	Inter-segment eliminations	Consolidated totals
Interest income	5,398	(1,751)	3,647
Interest expense	(55,630)	1,751	(53,879)
Depreciation and amortization	(81,306)	–	(81,306)
Impairment of property, equipment, and intangible assets	(16,438)	–	(16,438)
Income tax	(7,451)	–	(7,451)
Capital expenditure	115,824	–	115,824

Revenues from any individual customer do not reach 10% of total revenues of the Group.

As at December 31, 2012, Mercator Group included the following companies (figures in EUR 000 are based on audited reporting packages by companies reporting to the parent company):

SLOVENIA

Poslovni sistem Mercator, d.d. Slovenia	
Equity	**740,244**
Financial liabilities	**763,419**
Profit (loss) for the year	**(77,602)**
Revenue	**1,425,391**
Number of employees	**9,397**

Intersport ISI, d.o.o. Slovenia	**100.0%**
Equity	**15,182**
Financial liabilities	**8,923**
Profit (loss) for the year	**57**
Revenue	**48,281**
Number of employees	**326**

Modiana, d.o.o. Slovenia	**100.0%**
Equity	**4,920**
Financial liabilities	**16,511**
Profit (loss) for the year	**(5,300)**
Revenue	**45,178**
Number of employees	**526**

M-Tehnika, d.d. Slovenia	**100.0%**
Equity	**3,266**
Financial liabilities	**19,576**
Profit (loss) for the year	**(10,758)**
Revenue	**137,832**
Number of employees	**988**

M Energija, d.o.o. Slovenia	**100.0%**
Equity	**5,047**
Financial liabilities	**6,092**
Profit (loss) for the year	**(2,209)**
Revenue	**23,297**
Number of employees	**9**

Mercator IP, d.o.o. Slovenia	**100.0%**
Equity	**2,419**
Financial liabilities	**20**
Profit (loss) for the year	**143**
Revenue	**11,276**
Number of employees	**419**

Mercator - Emba, d.d. Slovenia	**100.0%**
Equity	**6,904**
Financial liabilities	**10,299**
Profit (loss) for the year	**403**
Revenue	**21,630**
Number of employees	**114**

M - Nepremičnine, d.o.o.** Slovenia	**100.0%**
Equity	**4,149**
Financial liabilities	**0**
Profit (loss) for the year	**78**
Revenue	**435**
Number of employees	**0**

Mercator - Optima, d.o.o. Slovenia	**100.0%**
Equity	**899**
Financial liabilities	**0**
Profit (loss) for the year	**(241)**
Revenue	**396**
Number of employees	**15**

SERBIA

Mercator - S, d.o.o. Serbia	**100.0%**
Equity	**215,193**
Financial liabilities	**110,166**
Profit (loss) for the year	**(3,371)**
Revenue	**545,142**
Number of employees	**4,525**

Intersport S-ISI, d.o.o. Serbia	**100.0%**
Equity	**1,375**
Financial liabilities	**2,052**
Profit (loss) for the year	**(170)**
Revenue	**8,318**
Number of employees	**117**

Modiana, d.o.o., Serbia Serbia	**100.0%**
Equity	**1,143**
Financial liabilities	**3,009**
Profit (loss) for the year	**(976)**
Revenue	**10,538**
Number of employees	**122**

CROATIA

Mercator - H, d.o.o. Croatia	**99.9%**
Equity	**151,974**
Financial liabilities	**174,349**
Profit (loss) for the year	**(61,879)**
Revenue	**336,234**
Number of employees	**3,041**

Intersport H, d.o.o. Croatia	**100.0%**
Equity	**4,573**
Financial liabilities	**5,804**
Profit (loss) for the year	**77**
Revenue	**25,460**
Number of employees	**238**

Modiana, d.o.o., Croatia Croatia	**100.0%**
Equity	**938**
Financial liabilities	**6,101**
Profit (loss) for the year	**(2,103)**
Revenue	**20,995**
Number of employees	**201**

Mercator centar tehnike, d.o.o. Croatia	**100.0%**
Equity	**(105)**
Financial liabilities	**1,154**
Profit (loss) for the year	**(2,103)**
Revenue	**8,904**
Number of employees	**147**

* Project-based real estate company which has not launched its activities yet.

BOSNIA AND HERZEGOVINA

Mercator - BH, d.o.o.	100.0%
Bosnia and Herzegovina	
Equity	34,245
Financial liabilities	43,516
Profit (loss) for the year	(3,167)
Revenue	146,107
Number of employees	1,515

Intersport BH, d.o.o.	100.0%
Bosnia and Herzegovina	
Equity	841
Financial liabilities	1,041
Profit (loss) for the year	30
Revenue	5,385
Number of employees	63

Modiana, d.o.o., Bosnia and Herzegovina	100.0%
Bosnia and Herzegovina	
Equity	1,270
Financial liabilities	1,202
Profit (loss) for the year	197
Revenue	7,137
Number of employees	77

M - BL, d.o.o.	100.0%
Bosnia and Herzegovina	
Equity	37,222
Financial liabilities	11,622
Profit (loss) for the year	1,160
Revenue	38,903
Number of employees	349

MONTENEGRO

Mercator - CG, d.o.o.	100.0%
Montenegro	
Equity	32,429
Financial liabilities	8,500
Profit (loss) for the year	37
Revenue	104,915
Number of employees	1,417

BULGARIA

Mercator - B, e.o.o.d.	100.0%
Bulgaria	
Equity	(22,083)
Financial liabilities	17,724
Profit (loss) for the year	(18,512)
Revenue	9,310
Number of employees	205

ALBANIA

Mercator - A, sh.p.k.	100.0%
Albania	
Equity	(7,419)
Financial liabilities	7,638
Profit (loss) for the year	(7,968)
Revenue	4,298
Number of employees	109

8. Business combinations and founding of new companies

Slovenia

In March 2012, the agreement became effective based on which the company Poslovni sistem Mercator, d.d., increased its shareholding in the company Vesna, Trgovsko podjetje, d.d., from 45.48 to 100 percent.

Strategic business combination had the following effect on the assets and liabilities of the Mercator Group on the day of acquisition:

EUR thousand	Note	Pre-acquisition carrying amounts	Fair value adjustments	Recognized values on acquisition
Property, plant, and equipment	14	2,933	1,709	4,642
Intangible assets	15	4	–	4
Deferred tax expenses	19	–	28	28
Loans and deposits		7	–	7
Available-for-sale financial assets	17	2	–	2
Inventories		296	–	296
Trade and other receivables		258	–	258
Cash and cash equivalents		24	–	24
Financial liabilities		(1,004)	(13)	(1,017)
Trade and other payables		(2,146)	–	(2,146)
Deferred tax liabilities	19	–	(335)	(335)
Net identifiable assets and liabilities		**374**	**1,389**	**1,763**
Excess of acquirer's interest in the net fair value of acquiree's identifiable assets and liabilities over cost	10			**1,349**
Consideration				414
Obtained cash				24
Cost of acquisition less obtained cash				390

Excess of acquirer's interest in the net fair value of acquiree's identifiable assets and liabilities over cost in the amount of EUR 1,349 thousand was de-recognized by the group through profit or loss for the current year.

The acquired operations of the company Vesna, d.d., generated revenue in the amount of EUR 2,898 thousand and earnings before taxes of EUR -435 thousand in the period from the day of takeover until the end of 2012, which also includes restructuring costs and the costs of the company's integration into the Group.

According to the opinion by an independent financial consultant on the justifiability of the transaction from the aspect of the company Mercator, d.d., and its shareholders, the transaction was, considering the relevant economic and financial terms and conditions, financially sound and appropriate.

As a part of the project of monetizing a part of the company's real estate, Poslovni sistem Mercator, d.d., also founded the following project-based real estate companies in 2012: Argentum - A, d.o.o., Argentum - B, d.o.o., Argentum - C, d.o.o., Argentum - D, d.o.o., Argentum - E, d.o.o., Argentum - F, d.o.o., Argentum - G, d.o.o., Argentum - H, d.o.o., in Argentum - I, d.o.o., by paying up share capital in the combined total of EUR 68 thousand. The monetization project has been temporarily postponed; the companies have not yet launched their business activities.

Croatia

In 2012, the company M – Tehnika, d.d., founded the company Mercator centar tehnike, d.o.o., with a contribution of share capital in the amount of EUR 3 thousand. On May 15, 2012, the company's capital was increased by EUR 2,000 thousand.

9. Revenue

Breakdown of revenue by categories

EUR thousand	2012	2011 restated
Sales of goods	2,716,910	2,718,402
Sales of services	140,065	138,773
Sales of products	24,989	21,052
Sales of materials	520	639
Expenses for discounts granted	(9,298)	(7,895)
Total	**2,873,186**	**2,870,971**

Sales of goods are also reduced by the amount of discounts to customers - Mercator Pika card holders.

10. Other income

EUR thousand	2012	2011 restated
Gain on sale of property, plant and equipment	1,756	6,997
Reversal of real estate impairment	375	–
Reversal of provisions	7,622	5,664
Excess of acquirer's interest in the net fair value of acquiree's identifiable assets and liabilities over cost	1,349	118
Other operating income	9,026	11,375
Total	**20,128**	**24,154**

Gains from disposal of property, plant and equipment, pertain to the disposal of non-core assets in Slovenia, amounting to EUR 1,515 thousand, and to the divestment of non-core assets in other markets in the amount of EUR 241 thousand.

With regard to revaluation of property to fair value, reversal of impairment in the amount of EUR 375 thousand was established and recognized.

Revenue from reversal of provisions pertains to the reversal of provisions for legal claims in the amount of EUR 4,959 thousand; use of assets/funds for disability contributions in the amount of EUR 2,406 thousand; and other revenue from reversal of provisions in the amount of EUR 257 thousand.

Excess of acquirer's interest in the net fair value of acquiree's identifiable assets and liabilities over cost in the amount of EUR 1,349 thousand pertains to the acquisition of the company TP Vesna, d.d.

The remaining part of the Group's other income includes indemnities based on insurance premiums and other indemnities in the amount of EUR 4,966 thousand; income from bonuses for hiring of persons with disabilities in the amount of EUR 808 thousand; and other operating income in the amount of EUR 3,252 thousand.

11. Expenses by nature

EUR thousand	2012	2011 restated
Depreciation of property, plant and equipment	74,097	71,745
Amortization of intangible assets	7,552	9,401
Depreciation of investment property	140	160
Labour costs (personnel expenses)	297,052	295,660
Cost of material	77,630	83,947
Costs of services excl. rents	166,721	164,996
Rental/lease costs	58,498	44,183
Cost of provisions	5,021	2,417
Other expenses	14,710	13,236
Impairment of property, equipment, and intangible assets	59,842	16,438
Loss from disposal of real estate	73	174
Change in the value of inventories	(298)	378
Other operating expenses	11,138	2,582
Cost of goods sold	2,163,285	2,112,967
Total cost of goods sold, selling costs and administrative expenses	**2,935,461**	**2,818,284**

Costs of goods sold, and selling costs in the amount of EUR 2,745,203 thousand (2011: EUR 2,704,991 thousand) pertain to production costs in the amount of EUR 30,782 thousand (2011: EUR 31,851 thousand); selling costs in the amount of EUR 540,296 thousand (2011: EUR 557,213 thousand); cost of goods sold in the amount of EUR 2,163,285 thousand (2011: EUR 2,112,967 thousand); changes in the value of inventories in the amount of EUR -298 thousand (2011: EUR 378 thousand); and other expenses in the amount of EUR 11,138 thousand (2011: EUR 2,582 thousand).

Recognition of provisions pertains to lawsuits in the amount of EUR 3,966 thousand; provisions for reorganization expenses in the amount of EUR 550 thousand; and other provisions in the amount of EUR 505 thousand.

Impairment of property, equipment, and intangible assets, and losses on sale of property, pertain to impairment on goodwill in the amount of EUR 5,885 thousand, impairment of brand in the amount of EUR 6,422 thousand, impairment to other intangible assets in the amount of EUR 555 thousand (Getro brand and IT licenses), impairment of real estate based on appraisal of fair value in the amount of EUR 35,118 thousand, write-downs of investments into foreign property, plant, and equipment in the amount of EUR 5,207 thousand related to the withdrawal form the Bulgarian market, write-downs of investments into foreign property, plant, and equipment in the amount of EUR 3,411 thousand related to the withdrawal form the Albanian market, write-down of investment in progress and investment into foreign property, plant, and equipment in Slovenia and in Croatia in the amount of EUR 3,230 thousand, and losses on disposal and deficits of property, plant, and equipment in the amount of EUR 87 thousand.

Other operating expenses pertain to accrued expenses for liquidated damages for termination of lease agreements in Bulgaria in the amount of EUR 6,581 thousand; accrued VAT payments related to write-downs of property, plant, and equipment in Albania in the amount of EUR 777 thousand; other penalties and damages in the amount of EUR 1,085 thousand; and expenses for recognition of provisions for retirement benefits and jubilee premiums in the amount of EUR 2,695 thousand.

Rental expenses include additional rents paid to lessors due to exit from the Albanian market in the amount of EUR 952 thousand.

In 2012, the Group's costs of services also include the costs of audit in the amount of EUR 325 thousand (2011: EUR 336 thousand). The auditors did not provide any other services.

Cost of goods sold is reduced by the rebates beyond accounts/invoices and received discounts. It is increased by revaluation adjustments to inventories in the amount of EUR 5,357 thousand, and write-downs of damaged, expired, and obsolete inventory and deficits in the total amount of EUR 15,320 thousand.

Revaluation adjustments to inventories include the adjustment resulting from the withdrawal from the markets of Bulgaria and Albania in the amount of EUR 449 thousand.

12. Personnel expenses

EUR thousand	2012	2011
Wages and salaries	217,846	220,756
Pension insurance costs	19,178	19,401
Health insurance costs	16,895	13,253
Termination benefits	2,335	274
Other labour costs	40,798	41,976
Total	**297,052**	**295,660**
Number of employees as at 31 December	23,920	24,266

Severance payments in the amount of EUR 580 thousand pertain to accrued expenses of exit from the markets of Bulgaria and Albania. In Slovenia, EUR 1,471 thousand of severance payments was paid out at the companies Mercator, d.d., M – Tehnika, d.d., and Modiana, d.o.o. In other markets, severance payments totalled at EUR 284 thousand.

Other labour costs include reinbursement meal allowances, commute allowances, holiday allowances, and other labour costs.

Average number of employees in the Group during the year calculated based on hours worked amounts to 22,770 (2011: 22,602).

13. Finance income and expenses

Finance income and expenses, recognized in profit or loss

EUR thousand	2012	2011
Interest income	3,374	3,647
Gains on disposal of subsidiaries	–	1,150
Gains on disposal of available-for-sale financial assets	280	–
Dividend income	113	56
Other finance income	1,012	846
Finance income	**4,779**	**5,699**
Interest expense	(50,939)	(53,879)
Losses on disposal and impairment of available-for-sale financial assets	(759)	(27)
Impairment of trade and other receivables	(11,198)	(5,301)
Net operating foreign currency translation differences	(3,043)	(1,027)
Net finance foreign currency translation differences	(6,320)	(2,356)
Other finance expense	(652)	(10)
Finance expenses	**(72,911)**	**(62,600)**
Net finance expense recognized in profit and loss	**(68,132)**	**(56,901)**

According to the Companies Act, referring to the breakdown of income statement, recognition and reversal of adjustments and collected receivables previously written off are defined as operating revenue or operating expense. In Groups view, these would be more reasonably defined as finance income and finance expenses as operating receivables are defined as non-derivative financial assets.

Revaluation adjustments and receivable write-downs pertain to revaluation adjustment to receivables from the Slovenian Tax Administration regarding the offset payment for meal allowance in the amount of EUR 2,046 thousand, and to revaluation adjustment to receivables in Serbia in the amount of EUR 3,362 thousand.

Finance income and expenses recognized in other comprehensive income (net)

EUR thousand	2012	2011
Foreign currency translation differences on consolidation	(18,544)	2,015
Net change in cash flow hedges	(898)	(2,224)
Net change in fair value of available-for-sale financial assets	3,514	(972)
Finance (expense) income recognized directly in comprehensive income	**(15,928)**	**(1,181)**
Attributable to:		
Parent company shareholders	(15,928)	(1,176)
Non-controlling interest	–	(5)
Finance (expense) income recognized in comprehensive income		
Recognized in:		
Fair value reserve	2,616	(3,196)
Currency translation reserve	(18,544)	2,020
Non-controlling interest	–	(5)
Total	**(15,928)**	**(1,181)**

14. Property, plant, and equipment

EUR thousand	Note	Land	Buildings	Production equipment	Office and other equipment	Construction in progress	Total
Balance at 1 January, 2011							
Cost		603,300	1,778,563	262,032	163,749	44,452	2,852,096
Accumulated depreciation		-	(698,039)	(176,967)	(106,662)	-	(981,668)
Carrying amount		**603,300**	**1,080,524**	**85,065**	**57,087**	**44,452**	**1,870,428**
Year ended 31 December, 2011							
Opening carrying amount		**603,300**	**1,080,524**	**85,065**	**57,087**	**44,452**	**1,870,428**
Effect of movements in exchange rates		(279)	1,687	241	24	24	1,697
Acquisitions through business combinations	8	508	7,478	6,217	-	545	14,748
Disposal of subsidiary		(2,381)	(1,845)	(688)	(302)	(58)	(5,274)
Additions		4,999	1,983	89	5,197	98,756	111,024
Transfers	15	472	71,475	16,978	12,820	(104,623)	(2,878)
Disposals		(6,142)	(3,626)	(218)	(418)	-	(10,404)
Depreciation charge	11	-	(44,874)	(14,725)	(12,146)	-	(71,745)
Impairment and write-offs		-	(728)	(850)	-	-	(1,578)
Closing carrying amount		**600,477**	**1,112,074**	**92,109**	**62,262**	**39,096**	**1,906,018**
Balance at 31 December, 2011							
Cost		600,477	1,836,001	264,057	175,867	39,096	2,915,498
Accumulated depreciation		-	(723,927)	(171,948)	(113,605)	-	(1,009,480)
Carrying amount		**600,477**	**1,112,074**	**92,109**	**62,262**	**39,096**	**1,906,018**
Year ended 31 December, 2012							
Opening carrying amount		**600,477**	**1,112,074**	**92,109**	**62,262**	**39,096**	**1,906,018**
Effect of movements in exchange rates		(5,391)	(19,688)	(1,884)	(862)	(485)	(28,310)
Acquisitions through business combinations	8	1,245	3,212	97	88	-	4,642
Additions		7,942	295	540	1,427	52,739	62,943
Transfers*	15	-	23,876	18,028	12,679	(54,047)	536
Disposals		(1,650)	(1,901)	(472)	(588)	(872)	(5,483)
Depreciation charge	11	-	(45,398)	(15,602)	(13,097)	-	(74,097)
Revaluation (value increases and impairments)		(43,622)	64,024	-	-	-	20,402
Write-offs		-	(8,770)	(1,725)	-	(1,421)	(11,916)
Closing carrying amount		**559,001**	**1,127,724**	**91,091**	**61,909**	**35,010**	**1,874,735**
Balance at 31 December, 2012							
Cost		559,001	1,945,822	267,305	178,188	35,010	2,985,326
Accumulated depreciation		-	(818,098)	(176,214)	(116,279)	-	(1,110,591)
Carrying amount		**559,001**	**1,127,724**	**91,091**	**61,909**	**35,010**	**1,874,735**

* Transfers are related to transfers between groups. Advance payments are included in construction in progress in the amount of EUR 285 thousand.

As at December 31, 2012, the Group held EUR 156,669 thousand of inactive property valued at fair value (2011: EUR 174,968 thousand). Inactive real property includes land intended for future development projects, and real property selected for divestment.

Investments in property, plant and equipment, which are recognized under investment, amounting to EUR 62,943 thousand, pertain to:

EUR thousand	2012
Additions of property, plant and equipment (new facilities)	36,794
Refurbishment of existing retail and wholesale units	23,490
Other	2,659
Total	**62,943**

Disposals of property, plant and equipment in the amount of EUR 5,483 thousand are related to the disposal of non-core assets. Proceeds from disposal amounted to EUR 7,166 thousand; gains from disposal were at EUR 1,756 thousand; losses from disposal amounted to EUR 73 thousand.

All land and buildings (property and plant) of the Group were appraised as at October 31, 2012. The appraisal was conducted based on market value as determined by an independent certified real estate appraiser.

The revaluation effect in 2012 is positive and it amounts to a total of EUR 20,402 thousand.

EUR thousand	Fair value reserve	Profit for the year	Total
value increases	73,570	–	73,570
reversal of value increases	(18,425)	–	(18,425)
impairments	–	(35,118)	(35,118)
reversal of impairments	–	375	375
Total effect on value of real estate	**55,145**	**(34,743)**	**20,402**

Write-offs of property, plant and equipment in 2012 amounted to EUR 11,916 thousand. They pertain to write-offs of investments into foreign property, plant and equipment upon withdrawal from the Bulgarian market in the amount of EUR 5,207 thousand; write-offs of investments into foreign property, plant and equipment upon withdrawal from the market of Albania in the amount of EUR 3,411 thousand; and write-offs of investment in progress and investment into foreign property, plant and equipment in Slovenia and in Croatia in the amount of EUR 3,298 thousand.

Depreciation of property, plant and equipment in the amount of EUR 74,097 thousand is included among costs of good sold in the amount of EUR 1,171 thousand, among the selling and marketing costs in the amount of EUR 67,032 thousand, and among the administrative expenses in the amount of EUR 5,894 thousand.

If land and buildings were stated on the historical cost basis, the amounts would be as follows:

EUR thousand	2012	2011
Cost	1,837,249	1,814,817
Revaluation adjustment	(457,995)	(417,115)
Carrying amount	**1,379,254**	**1,397,702**

Leased Property, plant, and equipment

Carrying amount of property, plant and equipment held under financial leases amounts to EUR 208,402 thousand (2011: EUR 222,562 thousand) and refers to land and buildings.

Security

As at December 31, 2012 the company had EUR 3,460 thousand of pledged real property.

15. Intangible assets

EUR thousand	Note	Goodwill	Trademarks, rights and licenses	Total
As at January 1, 2011				
Cost		9,984	78,846	88,830
Revaluation adjustment		–	(36,204)	(36,204)
Carrying amount		**9,984**	**42,642**	**52,626**
Year ended December 31, 2011				
Opening carrying amount		**9,984**	**42,642**	**52,626**
Effect of exchange rate movements		(171)	632	461
Acquisition through business combinations	8	–	861	861
Disposal of subsidiary		–	(52)	(52)
Investment		–	4,800	4,800
Disposals		–	(1)	(1)
Transfers		–	1	1
Impairment		(3,037)	(10,396)	(13,433)
Depreciation and amortization	11	–	(9,401)	(9,401)
Closing carrying amount (restated)		**6,776**	**29,086**	**35,862**
As at December 31, 2011				
Cost		6,776	61,979	68,755
Revaluation adjustment		–	(32,893)	(32,893)
Carrying amount (restated)		**6,776**	**29,086**	**35,862**
Year ended December 31, 2012				
Opening carrying amount		**6,776**	**29,086**	**35,862**
Effect of exchange rate movements		(4)	(1,427)	(1,431)
Acquisition through business combinations	8	–	4	4
Investment		–	4,382	4,382
Disposals		–	(16)	(16)
Impairment		(5,885)	(6,977)	(12,862)
Depreciation and amortization	11	–	(7,552)	(7,552)
Closing carrying amount		**887**	**17,500**	**18,387**
As at December 31, 2012				
Cost		887	52,026	52,913
Revaluation adjustment		–	(34,526)	(34,526)
Carrying amount		**887**	**17,500**	**18,387**

Intangible assets in development as at December 31, 2012 amount to EUR 152 thousand.

Intangible assets as at December 31, 2012 include rights, patents, licenses, trademarks, and investments into software in amount of EUR 17,500 thousand (2011: EUR 29,086 thousand); and goodwill in the amount of EUR 887 thousand (2011: EUR 6,776 thousand).

In 2011, impairment of intangible assets was adjusted pursuant to IAS 8 by EUR 9,851 thousand. Accounting error, amounting to EUR 9,851 thousand, occurred at the subsidiary Mercator-S, d.o.o., Serbia. It refers to the change in the value of an intangible asset arising from the right to rents that are more favourable than those offered on the market.

In 2012 the Getro brand was impaired by the amount of EUR 6,422 thousand, and the information technology licences were impaired by the amount of EUR 555 thousand.

Goodwill in the amount of EUR 887 thousand, generated in previous years, arises from the acquisition of companies Era Tornado, d.o.o, Croatia, and Trgohit, d.o.o., Croatia, in 2005.

Amortization in the amount of EUR 7,552 thousand was included among the production costs in the amount of EUR 24 thousand; among the selling and marketing costs in the amount of EUR 2,257 thousand; and among the administrative expenses in the amount of EUR 5,272 thousand.

Impairment testing of goodwill

Goodwill in the amount of EUR 4,360 thousand, which was created upon the acquisition of the company Presoflex, d.o.o., Croatia, was allocated to cash-generating units of the Group, defined according to the store format, and tested for impairment on December 31, 2012. In 2012, it was entirely impaired.

Goodwill in the amount of EUR 1,579 thousand, which was created in 2005 upon the acquisition of the companies Era Tornado, d.o.o., and Trgohit, d.o.o., in Croatia was allocated to cash-generating units of the Group, defined according to the store format; on December 31, 2012 it was tested for impairment. In 2012, impairment amounted to EUR 688 thousand.

Remaining goodwill in the amount of EUR 837 thousand, pertaining to various minor transactions, was not allocated to the Group's cash-generating units; it was impaired in entirety in 2012.

A summary of the goodwill allocation and impairment is presented below:

EUR thousand	December 31, 2011	Effect of exchange rates movements	Impairment in 2012	December 31, 2012
Hypermarkets	537	–	(537)	–
Supermarkets	4,987	(4)	(4,096)	887
Markets	407	–	(407)	–
Other stores	9	–	(9)	–
Unallocated	836	–	(836)	–
Total	**6,776**	**(4)**	**(5,885)**	**887**

When testing goodwill for impairment with regard to the acquisition of the company Presoflex, d.o.o., the recoverable amount of cash-generating unit was determined based on the calculations of value in use. The calculations are based on cash flow projections prepared against the background of business plans for the following year, and projected forwards upon appropriate assumptions. The main assumptions considered in the calculation of values in use include the following: revenue growth rate of 1.0% and discount rate of 9.5%. Gross cash flow from operating activities as percentage of sales revenue is defined based on operation and performance history, structure of sales, and expectations regarding the developments in the market. The discount rate applied is based on market rates, adjusted to reflect the specific risks related to the business units. Sensitivity analysis of the effect of assumptions used in the calculation on the values in use of cash-generating units was conducted for the purpose of goodwill impairment testing with regard to the company Presoflex, d.o.o. Risk of change in future expected changes of gross margin and change in parameters affecting the determination of the discount rate were found to have the largest effect on the estimated value of cash-generating units.

It was determined that the recoverable amount of cash-generating units is lower than their carrying amount, including the goodwill, therefore goodwill was impaired in amount of EUR 4,360 thousand.

When testing goodwill for impairment with regard to the acquisition of the companies Era Tornado, d.o.o., and Trgohit, d.o.o., the recoverable amount of cash-generating unit was determined based on the calculations of value in use. The calculations are based on cash flow projections prepared against the background of business plans for the following year, and projected forwards upon appropriate assumptions. The main assumptions considered in the calculation of values in use include the following: revenue growth rate of 1.0% and discount rate of 9.5%. Gross cash flow from operating activities as percentage of sales revenue is defined based on operation and performance history, structure of sales, and expectations regarding the developments in the market. The discount rate applied is based on market rates adjusted to reflect the specific risks related to the business units. Sensitivity analysis of the effect of assumptions used in the calculation on the values in use of cash-generating units was conducted for the purpose of goodwill impairment testing with regard to the companies Era Tornado, d.o.o., and Trgohit, d.o.o. Risk of change in future expected changes of gross margin and change in parameters affecting the determination of the discount rate were found to have the largest effect on the estimated value of cash-generating units.

It was determined that the recoverable amount of cash-generating units is lower than their carrying amount, including the goodwill, therefore goodwill was impaired in amount of EUR 688 thousand.

Impairment to goodwill amounted to a total of EUR 5,885 thousand, of which EUR 4,360 thousand pertains to goodwill impairment from the acquisition of the company Presoflex, d.o.o.; EUR 688 thousand pertains to goodwill impairment from acquisitions of companies Era Tornado, d.o.o., and Trgohit, d.o.o.; and EUR 837 thousand pertains to goodwill impairment from various minor transactions.

16. Investment property

EUR thousand	2012	2011
As at Jan 1	**3,450**	**3,894**
Investment	5	–
Transfer from property, plant, and equipment	5	12
Disposals	(126)	(296)
Depreciation and amortization	(140)	(160)
As at December 31	**3,194**	**3,450**
Balance at 31 December		
Cost	6,855	7,303
Revaluation adjustment	(3,661)	(3,853)
Carrying amount	**3,194**	**3,450**

Fair value of investment property as at December 31, 2012, amounts to EUR 8,685 thousand (2011: EUR 9,360 thousand).

Disposals and proceeds from disposals of investment property amount to EUR 126 thousand.

The following amounts were recognized in the income statement with regard to investment property:

EUR thousand	2012	2011
Rental income	223	233
Direct operating expenses arising from investment properties that generate rental income	(216)	(236)
Total	**7**	**(3)**

Depreciation of investment property in the amount of EUR 140 thousand was included among the cost of sales.

17. Available-for-sale financial assets

EUR thousand	2012	2011
As at Jan 1	**2,628**	**3,959**
Effect of exchange rates movements	–	(5)
Acquisition through business combinations	2	–
Acquisitions of shares and interests	9	10
Changes in fair value	(149)	(1,235)
Disposal of subsidiary	–	(101)
Disposals	(1,421)	–
As at December 31st	**1,069**	**2,628**

The Group's available-for-sale financial assets also include assets that could not be valued at fair value; thus, these assets are measured at historical costs. Shares of these companies are not listed or traded in the stock market. The Group estimates that costs of evaluating the fair value of all these financial assets would have been too high, while the evaluation would not considerably affect the correctness of financial statements.

EUR thousand	2012	2011
Available-for-sale financial assets measured at cost	731	743
Available-for-sale financial assets measured at fair value	338	1,885
Total equity securities and shares	**1,069**	**2,628**

As at December 31, 2012, the Group does not hold any financial assets at fair value through profit or loss, or held-to-maturity investments.

18. Derivative financial instruments

EUR thousand	2012	2011
Assets		
Interest rate caps	1	158
Liabilities		
Interest rate swaps	(5,269)	(4,562)

The carrying amounts of derivative financial instruments equal fair values.

The nominal amount of borrowings hedged from interest rate risk as at December 31, 2012 amounted to EUR 350,000 thousand; the Group held interest rate swaps in the amount of EUR 175,000 thousand (contracted interest rates varied between 2.127% and 2.521%) and interest rate caps in the amount of EUR 175,000 thousand with a strike rate of 3.50%. All derivative financial instruments were acquired in 2011, for a period of three years. As at December 31, 2012, the relevant floating interest rate, i.e. the 6-month EURIBOR, amounted to 0.32%. Derivative financial instruments held by the Group are intended for cash flow hedging.

As at December 31, 2012, the Group did not hold any derivative financial instruments intended for hedging fair value.

Other than interest rate swaps and interest rate caps, the Mercator Group did not hold any other contracts with third parties that represent derivative financial instruments as at December 31, 2012.

19. Taxes

Taxes recognized in profit or loss

EUR thousand	2012	2011 restated
Current tax expense	144	8,573
Deferred tax	(5,803)	(1,122)
Tax	**(5,659)**	**7,451**

In 2012 income tax liability of the companies in the Mercator Group amounts to EUR 144 thousand.

According to IAS 12 current tax and deferred tax are recognized as revenue or expense and are included in profit or loss. If tax relates to items recognized in equity, deferred tax is also recognized directly in equity.

Tax recognized in other comprehensive income

EUR thousand	2012		
	Value before tax	Income tax expense	Value after tax
Change in fair value of real estate	55,145	(5,034)	50,111
Change in fair value of available-for-sale financial assets	(89)	20	(69)
Disposal of available-for-sale financial assets.	699	(166)	533
Change in fair value of equity investment in subsidiaries	–	3,032	3,032
Change in fair value of instruments held for hedging	(864)	(34)	(898)
Foreign currency translation differences on consolidation	(18,544)	–	(18,544)
Other changes -	–	(414)	(414)
Other comprehensive income	**36,347**	**(2,596)**	**33,751**

Change in fair value of investments into equity of subsidiaries includes deferred taxes related to revaluation adjustments to these investments.

EUR thousand	2011		
	Value before tax	Income tax expense	Value after tax
Real property disposal and depreciation	–	186	186
Change in fair value of available-for-sale financial assets	(1,208)	236	(972)
Change in fair value of cash flow hedges	(2,780)	556	(2,224)
Foreign currency translation differences on consolidation	2,015	–	2,015
Other comprehensive income	**(1,973)**	**978**	**(995)**

Reconciliation to effective tax rate

EUR thousand	**2012**	**2011 restated**
Profit (loss) for the year	(104,620)	12,489
Tax	(5,659)	7,451
Profit before income tax	(110,279)	19,940
Tax calculated at 18% (20%) tax rate	(19,850)	3,988
Tax on income that increases the tax base	411	(134)
Tax on income that decreases the tax base	(599)	(3)
Tax of non-deductible expenses	1,688	1,395
Effect of current losses for which deferred tax was not recognized	12,379	3,115
Tax relief	(110)	(1,514)
Effect of different tax rates and other	423	604
Total income tax expense	**(5,659)**	**7,451**
Effective tax rate	**–**	**37.4%**

Deferred taxes are calculated based on temporary differences under the liability method, by applying the tax rate effective in individual countries of the Mercator Group's operations.

The movement in the deferred tax ballances is as follows:

EUR thousand	2012	2011 restated
At beginning of year – net deferred tax assets (liabilities)	**(36,071)**	**(39,595)**
Change in accounting policy	–	(37)
Effect of exchange rates movements	430	(51)
Acquired in a business combination	(307)	377
Disposal of subsidiary	–	503
Recognized in profit or loss	5,803	1,122
Recognized in other comprehensive income	(2,596)	978
Recognized in liabilities	479	632
At end of year – net deferred tax assets (liabilities)	**(32,262)**	**(36,071)**

The deferred tax assets and liabilities are attributable to the following items:

Deferred tax liabilities

EUR thousand	Revaluation of property, plant and equipment	Revaluation adjustments to available-for-sale financial assets and derivative financial instruments	Depreciation of property, plant and equipment under EUR 500	Difference between tax recognized and business depreciation	Total
As at January 1, 2011	**49,166**	**65**	**853**	**1,185**	**51,269**
Effect of exchange rates movements	(67)	–	–	20	(47)
Acquired in a business combination	73	–	–	–	73
Disposal of subsidiary	(503)	–	–	–	(503)
Recognized in profit or loss	(7)	–	10	(1,065)	(1,062)
Recognized in other comprehensive income	(188)	(65)	–	–	(253)
Recognized in liabilities	(632)	–	–	–	(632)
As at December 31, 2011, restated	**47,842**	**–**	**863**	**140**	**48,845**
Effect of exchange rates movements	(283)	–	–	(25)	(308)
Acquired in a business combination	335	–	–	–	335
Transfers among items	(510)	–	–	510	–
Recognized in profit or loss	(144)	–	(272)	444	28
Recognized in other comprehensive income	5,034	5	–	414	5,453
Recognized in deferred tax assets	(1,234)	–	–	–	(1,234)
Recognized in liabilities	(592)	113	–	–	(479)
As at December 31, 2012	**50,448**	**118**	**591**	**1,483**	**52,640**

Deferred tax assets

EUR thousand	Provisions not recognized for tax purposes	Impairment of trade receivables	Temporary difference due to change in accounting policies	Tax loss	Impairment of inventory	Differences between tax recognized and business depreciation	Change in fair value of available-for-sale financial assets and derivatives	Other	Total
As at January 1, 2011	**3,071**	**1,766**	**2,974**	**–**	**337**	**2,073**	**1,263**	**190**	**11,674**
Change in accounting policy	–	–	(37)	–	–	–	–	–	(37)
Effect of exchange rates movements	–	–	–	–	(6)	(41)	–	(51)	(98)
Acquired in business combinations	–	–	–	–	–	–	–	450	450
Recognized in profit or loss	(575)	(4)	–	–	(25)	376	–	288	60
Recognized in other comprehensive income	–	–	–	–	–	–	725	–	725
As at December 31, 2011	**2,496**	**1,762**	**2,937**	**–**	**306**	**2,408**	**1,988**	**877**	**12,774**
Reversal of temporary difference due to change in accounting policies	–	–	(2,937)	2,937	–	–	–	–	–
Effect of exchange rates movements	(0)	1	–	–	–	(1)	122	–	122
Acquired in a business combination	–	–	–	–	–	28	–	–	28
Transfers between items	–	–	–	779	–	–	–	(779)	–
Recognized in profit or loss	1,007	70	–	557	(242)	(69)	(211)	4,719	5,831
Recognized in deferred tax liabilities	–	–	–	(1,234)	–	–	–	–	(1,234)
Recognized in other comprehensive income	–	–	–	3,036	–	–	(179)	–	2,857
As at December 31, 2012	**3,503**	**1,833**	**–**	**6,075**	**64**	**2,366**	**1,720**	**4,817**	**20,378**

As at December 31, 2012, the Group holds unrecognized deferred assets from tax losses in the amount of EUR 17,328 thousand (2011: EUR 4,949 thousand). These pertain especially to tax losses of the companies Mercator-H, d.o.o., Mercator - B, e.o.o.d., M - Tehnika, d.d., and Mercator - A, sh.p.k.

In 2012 companies of Mercator Group have recognized deferred tax liabilities as well as deferred tax assets. Deferred tax liabilities charged to the income statement decrease tax bases of individual companies of the Group in 2012, whereas the deferred tax assets increase them.

Deferred tax assets not recognized through profit or loss, pertaining to the revaluation of equity investment into subsidiary Mercator-H, d.o.o., amounted to EUR 6,371 thousand. Deferred tax assets not recognized in comprehensive income were related to revaluation of investment into equity of subsidiaries Mercator - S, d.o.o., Mercator - CG, d.o.o., M - BL, d.o.o., M - Energija, d.o.o., and Mercator - BH, d.o.o., and they amounted to EUR 2,180 thousand. These deferred tax assets were not recognized because the parent company does not intend to dispose of the said subsidiaries in the foreseeable future.

Deferred tax assets and liabilities are not offset in the balance sheet.

20. Inventories

EUR thousand	2012	2011 restated
Merchandise	285,458	322,681
Material	4,943	5,116
Work in progress	18	12
Finished goods	1,374	857
Less: revaluation adjustment of inventories	(24,082)	(18,725)
Total	**267,711**	**309,941**

Inventories of trade goods/merchandise, raw and processed materials, work in progress, and finished products as at December 31, 2012 amounted to EUR 267,711 thousand, which is 13.6% less than at the beginning of the year. The decrease in inventory is mostly a result of proactive policy of working capital management. Increase in the revaluation adjustment of inventories mostly pertains to the home product program, apparel program, and Intersport, as well as to revaluation adjustments related to the withdrawal from the markets of Bulgaria and Albania.

21. Trade and other receivables

EUR thousand	2012	2011
Trade receivables	224,684	226,919
Deferred costs	7,434	7,572
Accrued revenues	7,880	8,911
Total trade and other receivables	**239,998**	**243,402**

Trade and other receivables dropped by EUR 598 thousand.

As at December 31, 2012 Mercator Group does not have any trade and other receivables from associated parties.

Deferred costs in 2012 amount to EUR 7,434 thousand, which is EUR 138 thousand less than in the year before, mostly due to decrease of accrued or deferred banking costs for the syndicated loan and deferred cost of insurance premiums.

Uncharged revenue pertains to anticipated and included rebates and compensations.

Carrying amounts of all trade and other receivables are in materially relevant sums consistent with their respective fair values. Receivables are measured at amortized cost.

The amount of impairment of receivables as at December 31, 2012 amounted to EUR 39,078 thousand (2011: EUR 36,270 thousand). Movements of the provision for impairment of trade receivables are presented in Note 29 (Financial instruments).

22. Loans and deposits

EUR thousand	2012	2011
Non-current deposits for rent payment	46,109	61,165
Loans to other companies	4,475	5,643
Deposits in banks	2,289	1,016
Total loans and deposits	**52,873**	**67,824**

Non-current deposits for rent payment relate to paid in advance rents for trade facilities abroad and are charged with interests. They are insured by mortgages on trade facilities. Loans granted to other companies mostly pertain to short-term loans to companies that have built or are still building trade facilities; these loans are secured by a mortgage on the property being developed.

23. Cash and cash equivalents

EUR thousand	2012	2011
Cash and cash equivalents	38,012	27,540

Cash in the amount of EUR 38,012 thousand includes cash in banks, cash in transit (daily proceeds of retail units), cash in hand, and foreign currency letters of credit.

24. Equity

Share capital
Share capital of the company Mercator, d.d., amounts to EUR 157,128,514.53. It is divided into 3,765,361 ordinary shares.

Conditional capital increase
Shareholders' Assembly of the company Poslovni sistem Mercator, d.d., can adopt a resolution on conditional capital increase on the basis of provisions stated in 46th article of the company Articles of Association; such possibility has not been realized so far.

Treasury shares
As at December 31, 2012 the company Poslovni sistem Mercator, d.d., held 42,192 treasury shares in the amount of EUR 3,235 thousand (2011: 42,192 treasury shares; EUR 3,235 thousand).

Reserves

Reserves consist of the share premium, revenue reserves, fair value reserve and currency translation reserve. None of those types of reserves can be used for the payment of dividends or other participations in profit.

Share premium amounts to EUR 198,872 thousand as at December 31, 2012. It includes the excess over nominal value of paid-up shares and surplus that was created as the difference between purchase and sales values of disposed treasury shares.

Revenue reserves, amounting to EUR 197,045 thousand as at December 31, 2012, include legal reserves, reserves for treasury shares, and other revenue reserves.

As at December 31, 2012, the Group holds legal reserves in the amount of EUR 13,389 thousand. Share premium and legal reserves can be used in surplus amount to increase the share capital from company assets, and for covering the net loss of the business year, or to cover the carried forward net loss, if revenue reserves are not used simultaneously to pay dividends to the shareholders.

As at December 31, 2012, the Mercator Group held 42,192 treasury shares in the amount of EUR 3,235 thousand. The reserve for treasury shares is reported among other revenue reserves.

Other revenue reserves as at December 31, 2012 amount to EUR 180,421 thousand. They include reallocated residuals of retained earnings from previous years. They can be used for any purpose, except for the amount of the reserve for treasury shares within other revenue reserves.

Currency translation reserve, amounting to EUR -78,819 thousand as at December 31, 2012, has decreased by EUR 18,544 thousand in 2012, which is related to an decrease due to currency translation differences that occurred upon the integration of financial statements of foreign subsidiaries into the consolidated financial statements.

Fair value reserve which amounts to EUR 240,762 thousand as at December 31, 2012, includes the revaluation reserve of property as measured by the revaluation model, changes to the fair value of available-for-sale financial assets, and changes to the value of effective cash flow hedges.

Fair value reserve is shown below:

EUR thousand	2012	2011
Real property fair value reserve	243,410	197,472
Fair value reserve for available-for-sale financial assets	3,084	(431)
Hedging reserve	(5,732)	(4,832)
Total fair value reserve	**240,762**	**192,209**

Dividends

Shareholders' Assembly adopted a resolution to pay dividends in 2012 in total amount of EUR 22,592 thousand (2011: EUR 30,123 thousand), or EUR 6.0 of gross dividend per share (2011: EUR 8.0 gross per share). Since the company Mercator, d.d., also included the 42,192 treasury shares in the calculation of dividends payout, an amount of EUR 253 thousand related to treasury shares was transferred back to retained earnings. Therefore undistributed profit of the year for the purposes of dividend payout was actually decreased to EUR 22,339 thousand (2011: EUR 29,785 thousand).

Due to negative results in 2012, dividend payment is not planned for 2013.

Other comprehensive income

EUR thousand	Fair value reserve: Revaluation reserve of property	Fair value reserve: Fair value reserve of available-for-sale financial assets	Fair value reserve: Hedging reserve	Retained earnings	Currency translation reserve	Total other comprehensive income attributable to owners of the parent company	Non-controlling interests	Total other comprehensive income
2012								
Revaluation of property	55,137	–	–	–	–	55,137	8	55,145
Disposal and depreciation of revalued property	(3,861)	–	–	3,861	–	–	–	–
Change in fair value of cash flow hedges	–	–	(864)	–	–	(864)	–	(864)
Change in fair value of available-for-sale financial assets	–	(89)	–	–	–	(89)	–	(89)
Disposal of available-for-sale financial assets.	–	699	–	–	–	699	–	699
Deferred tax	(5,339)	2,904	(34)	(125)	–	(2,594)	(2)	(2,596)
Foreign currency translation differences – foreign operations	–	–	–	–	(18,544)	(18,544)	–	(18,544)
Total other comprehensive income	**45,937**	**3,514**	**(898)**	**3,736**	**(18,544)**	**33,745**	**6**	**33,751**
2011								
Disposal and depreciation of revalued property	(3,671)	–	–	3,671	–	–	–	–
Change in fair value of cash flow hedges	–	–	(2,780)	–	–	(2,780)	–	(2,780)
Change in fair value of available-for-sale financial assets	–	(1,208)	–	–	–	(1,208)	–	(1,208)
Deferred tax	845	236	556	(659)	–	978	–	978
Foreign currency translation differences – foreign operations	–	–	–	–	2,020	2,020	(5)	2,015
Total other comprehensive income	**(2,826)**	**(972)**	**(2,224)**	**3,012**	**2,020**	**(990)**	**(5)**	**(995)**

25. Earnings per share

Basic earnings per share are calculated by dividing the net profit attributable to shareholders by the weighted average number of ordinary shares in issue during the year, excluding the average number of treasury shares.

	2012	2011 restated
Profit attributable to the owners of the parent company (EUR thousand)	(104,555)	12,506
Weighted average number of ordinary shares	3,723,169	3,723,169
Basic (loss) earnings per share in EUR	**(28.1)**	**3.4**

	2012	2011
Issued ordinary shares at January 1	3,765,361	3,765,361
Effect of treasury shares	(42,192)	(42,192)
Weighted average number of ordinary shares at December 31	**3,723,169**	**3,723,169**

Since the Group does not have any preference shares or convertible bonds, diluted net loss per share are the same as basic net loss per share.

26. Borrowings and other financial liabilities

EUR thousand	2012	2011
Non-current financial liabilities		
Bank borrowings	410,598	613,820
Finance lease	183,243	208,315
Borrowings from other companies	–	10
Total	**593,841**	**822,145**
Current financial liabilities		
Bank borrowings	220,144	146,447
Borrowings from other companies	19,739	16,441
Current portion of finance lease liabilities	25,159	14,247
Current portion of bank borrowings	235,837	185,453
Total	**500,879**	**362,588**
Total financial liabilities	**1,094,720**	**1,184,733**

In debt management, Mercator Group considered the increase in refinancing risk in financial markets and signed with the majority of banks an agreement to establish a new long-term structure of financing sources by mid 2013. One of the key elements of the final agreement which is to be based on aligning cash flows available for debt repayment with financial liabilities, will be hedging of refinancing risk, which will improve Mercator Group's financial stability.

Issue of short-term commercial papers has become another important financing source in 2012. In 2012, Mercator made 4 issues of 6-month commercial papers, amounting from EUR 5 million to 12 million.

As at December 31, 2012 the company had EUR 3,460 thousand of pledged real property.

Effective interest rates as at the cut-off date of balance sheet:

	2012	2011
Bank borrowings	3.93%	4.53%
Other borrowings	2.70%	3.66%

Floating interest rates are mostly interest rates related to EURIBOR. Average 6-month EURIBOR was lower in 2012 than in the year before by 0.81 percentage point.

Fixed interest rates are mostly related to borrowings from domestic banks, with fixed nominal interest rate. Financial liabilities are hedged with the use of derivative financial instruments, i.e. by interest rate swaps and caps.

Financial covenants

Financial covenants are uniform for all financial liabilities and they are represented by three indicators: ratio between net financial liabilities and equity (financial leverage indicator); ratio between gross cash flow from operating activities and net interest expense (interest coverage ratio); and amount of Group equity.

The Management Board was in the process of negotiations with its banking partners because the Group failed to attain at the end of the first half of 2012 and as at December 31, 2012 the minimum value of the interest coverage ratio (ratio between gross cash flow from operating activities/EBITDA and net interest expense), and exceeded the maximum value of the financial leverage indicator (ratio between net financial liabilities and equity). The Management Board was granted waivers for these covenants.

Finance lease liabilities

Finance lease liabilities - minimum lease payments:

EUR thousand	Future minimum lease payments	Interest	Present value of minimum lease payments	Future minimum lease payments	Interest	Present value of minimum lease payments
	2012	**2012**	**2012**	**2011**	**2011**	**2011**
Less than one year	30,761	5,602	25,159	22,693	8,427	14,266
Between one and five years	111,484	12,856	98,628	128,762	23,137	105,625
More than five years	91,219	6,604	84,615	115,797	13,126	102,671
Total	**233,464**	**25,062**	**208,402**	**267,252**	**44,690**	**222,562**

Mercator Group has also employed finance lease as a method of financing its major trade facilities in Slovenia and Croatia, and some land in Slovenia. Finance leases are signed for periods of 5 to 20 years; the last such lease is to expire in 2026.

Carrying amounts of all financial liabilities approximate their fair values. The share of non-current financial liabilities in total financial liabilities as at December 31, 2012 amounted to 54% (69% as at December 31, 2011).

27. Provisions

EUR thousand	Restitution claims	Restructuring provisions	Legal claims	Retirement benefits and jubilee premiums provisions	Other provisions	Total
As at January 1, 2012	**1,348**	**40**	**12,189**	**18,821**	**313**	**32,711**
Increase	371	728	4,924	1,085	2,295	9,403
Utilization	(1,114)	–	(19)	(1,786)	(2,406)	(5,325)
Reversal	(234)	(23)	(4,959)	–	–	(5,216)
Effect of exchange rates movements	–	–	(10)	(104)	–	(114)
As at December 31, 2012	**371**	**745**	**12,125**	**18,016**	**202**	**31,459**

Compared to the end of 2011, total provisions are lower by EUR 1,252 thousand.

Total increase of EUR 9,403 thousand includes revaluation adjustments upon regular annual assessment of provisions recognized in previous years in the amount of EUR 2,087 thousand to be debited to revenue, and newly recognized provisions, reported in operating costs, in the amount of EUR 7,316 thousand, of which EUR 2,295 thousand is to be debited to labour costs (provisions for improvement of working conditions for employees with disabilities), and

EUR 5,021 thousand is to be debited to long-term provisions.

Provisions debiting the liabilities decreased by EUR 2,919 thousand; provisions crediting other operating income decreased by EUR 7,622 thousand; currency translation differences amount to EUR -114 thousand. Net effect on the income statement amounted to EUR -1,781 thousand.

Provisions for restitution claims
Restitution claims as at December 31, 2012 amount to EUR 371 thousand. Compared to the year before, this liability is lower by EUR 977 thousand. New provisions were recognized in the amount of EUR 371 thousand. Restitution beneficiaries were paid liabilities in the total amount of EUR 1,114 thousand; EUR 234 thousand of long-term provisions for restitution claims were reversed and added to revenue.

Provisions for reorganization costs
As at December 31, 2012 provisions for reorganization expenses amount to EUR 745 thousand, which is EUR 705 thousand more than last year. Additional provisions were recognized in 2012 in a total amount of EUR 728 thousand, of which EUR 394 thousand at the company M - Tehnika, d.d.; EUR 156 thousand at Mercator - H, d.o.o.; EUR 73 thousand at Mercator - S, d.o.o.; EUR 66 thousand at Modiana - H, d.o.o.; and EUR 39 thousand at Intersport - H, d.o.o. Long-term provision was decreased by payments in the amount of EUR 23 thousand.

Legal claims
In 2012 provisions for legal claims were decreased by EUR 64 thousand. Based on received legal claims and legal opinion, the Group recognized additional provisions in the total amount of EUR 4,924 thousand in 2012. Following the completion of legal proceedings decided in favour of Mercator, provisions in the amount of EUR 4,959 thousand were reversed, and EUR 19 thousand of liabilities were paid to plaintiffs. Decrease of EUR 10 thousand pertains to currency translation differences.

Retirement benefits and jubilee premiums provisions
As at December 31, 2012, the value of provisions for retirement benefits and jubilee premiums amounted to EUR 18,016 thousand; currency translation differences amount to EUR -104 thousand. Compared to the year before, provisions are lower by EUR 805 thousand. In 2012, additional provisions of EUR 1,085 thousand were recognized, and payment of retirement benefits, severance pays, and jubilee bonuses has been debited to provisions in the total amount of EUR 2,406 thousand. The difference is included in other operating revenue for the current year.

Other provisions
Compared to the year 2011, other provisions are lower by EUR 111 thousand. The differences pertain to provisions for improvement of working conditions of persons with disabilities at the companies Mercator, d.d., Mercator IP, d.o.o., Intersport, d.o.o., and Modiana, d.o.o. In 2012, they were increased by EUR 2,259 thousand. They were drawn and reversed pursuant to relevant legislation in the amount of EUR 2,406 thousand, to cover the labour costs of persons with disabilities, labour costs of employees helping the persons with disabilities, and depreciation to property, plant and equipment related to the work of persons with disabilities.

28. Trade and other payables

EUR thousand	2012	2011
Trade payables	588,491	509,393
Payables to employees	21,246	20,842
Social security and other taxes	14,720	11,478
Other payables	3,756	4,464
Accrued costs	31,638	23,710
Deferred revenues	15,469	16,464
Total	**675,320**	**586,351**
Trade and other payables include:		
Non-current/long-term payables	2,462	2,369
Current/short-term payables	672,858	583,982

Accrued expenses pertain to accrued interest paid on borrowings, rebates granted but not accounted for, and compensations/reimbursements; and to accrued expenses of withdrawal from the markets of Bulgaria and Albania.

Deferred revenue includes particularly deferred revenue for claiming the discounts related to Mercator Pika bonus points.

Trade payables in 2012 are higher by EUR 88,969 thousand, which is mostly the result of the managing policy regarding trade payables and current financial liabilities.

As at December 31, 2012, Mercator Group does not have any liabilities towards the members of the Supervisory Board, while liabilities towards Management Board members and other employees include recognized undisbursed compensation for December 2012.

29. Financial instruments

Financial risk management

(a) Risk overview

The Group is monitoring and controlling different types of financial risks to which its operations are exposed:

- credit risk,
- liquidity risk,
- market risk.

Market risk management involves managing the interest rate and currency risk. The Group's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Group's financial performance.

This note presents the information on the Group's exposure to the risks listed above, as well as the goals, policies, and processes for measurement and management thereof and the Group's equity.

(b) Risk management policy

Active risk management at the Mercator Group pursues the objective of timely recognition and response to potential threats by developing appropriate measures to hedge against identified risks or to reduce risk exposure. The parent company manages interest rate, currency and liquidity risks centrally for the entire Group, whereas credit risks are managed as a rule by subsidiaries. Risk management measures are incorporated into daily operations at all companies of the Mercator Group.

Risk management activities at Mercator Group are the responsibility of the dedicated Risk Management Council. The council is managing a systematic risk management process which is laid down in the Rules of Procedure for Risk Management. Since the risks are monitored and managed from the aspect of several professional fields, Risk Management Committees, covering three main fields of risks, were founded to provide support to the Risk Management Council. Risk management is a central corporate function managed and coordinated by the company Mercator, d.d.

Mercator Group manages financial risks in the framework of adopted policy centrally at the parent company level which enters into interest rate swap contracts at market terms (arm's length principle) based on specific policies for managing specific risks.

Risks occurring in the process of compilation and development of financial statements are managed by employment of clear and concise accounting practices and their strict implementation; efficient organization of the accounting function; and regular internal and external audits and reviews of internal controls, business processes, and operations.

Pursuant to the Companies Act, audit of financial statements is mandatory for the Mercator Group. The purpose of the audit is to increase the level of trust among the users of financial information. The auditor applies appropriate audit procedures and methods to review the financial statements and passes an opinion as to whether they are compiled in compliance with the appropriate framework of financial reporting in all relevant aspects.

Internal audit has been in operation at the Mercator Group as an independent support function since 2000. The basic function of internal audit is perpetual development and monitoring of the internal control systems from the aspect of management, or hedging, of all sorts of operating and other risks to which the Group is exposed.

Quality performance of the supervisory function by the Supervisory Board of the company Mercator, d.d., is also supported by the Audit Committee which, among other duties, is in charge of supervising the operation of the risk management system, internal audit and the internal control system, and takes part in specifying the major auditing areas and the selection of the independent third-party auditor for the Group companies.

At Mercator Group, we are constantly studying and analyzing the existing and potential new risks, and implementing measures to manage, or hedge them.

Risk management process includes risk identification, sensitivity analysis, determination of threshold for key risks, taking measures to control risks and the implementation of these in the everyday decision-making in individual areas.

Estimates of exposure to individual risk types are prepared according to the probability and an assessment of damages in case of certain events. Exposure to risks is assessed based on sensitivity analysis which identifies by how much the gross cash flow from operating activities at the level of the Group or a particular company would drop in case of occurrence of a particular event taken as the basis for risk analysis. Probability is calculated based on analysis of data on past events, and expectations on the frequency of individual events in the year ahead. The analysis includes different effects and factors adjusted to particular types of risk.

Risks that cannot be quantified are assessed qualitatively. Estimated key risks, that exceed 1% of gross cash flow from operating activities of the Group or individual company, and for them no measures have been taken so far or they are not hedged in a manner that the risk would be entirely controlled, are most closely monitored and managed with measures, that either minimize the damage at the occurrence of an event, or reduce the level of likelihood of occurrence of an event, thus mitigating the risk to an acceptable level. Implementation of the measures adopted for managing the key risks is reviewed by a special internal audit, and reported to the Audit Committee on a quarterly basis.

Mercator Group performance in 2012 was considerably affected by aggravated conditions in global financial markets, which bore a negative impact on the entire economic environment both globally and in the markets of Mercator operations. This was reflected in notable drop in retail demand, as well as in the persistence of the trend of uncertainty with regard to financial risks which were not common in the period before the crisis. In such harsh and uncertain environment, it was crucial for Mercator Group to carefully manage the risks that it faces in its business operations.

Credit risk

Credit risk is the risk that the Group will suffer financial loss if a party to an agreement defers a payment and later does not settle its obligations in full or not at all. Credit risk arises mainly from receivables to wholesale customers and receivables from Mercator Pika card.

Group's exposure to credit risk is particularly dependent on the characteristics of individual customers. However, Mercator Group's exposure to customers is highly dispersed. In accordance with the adopted policy for each new customer, an analysis of its creditworthiness is performed before the Group offers its standard payment terms. The analysis of the Group's credit rating includes external ratings and assessments, if they exist. Limits on purchases, which represent the maximum amount of open positions, are determined for each customer individually. Group's business with customers who do not meet the benchmark credit rating shall take place only on the basis of advance payments or subject to appropriate payment insurance.

The carrying amounts of financial assets (receivables and loans) represent the maximum credit exposure. The maximum exposure to credit risk at the reporting date was:

EUR thousand	2012	2011
Trade and other receivables	239,998	243,402
Non-current deposits for rent payment	46,109	61,165
Loans to other companies	4,475	5,643
Deposits in banks	2,289	1,016
Total	**292,871**	**311,226**

Trade receivables derive from wholesale of goods, material, and services, and sale of goods to individuals, Mercator Pika card holders. Both wholesale and retail customers are dispersed; hence, there is no major exposure to an individual customer. The Group is also constantly monitoring customer payment defaults and checks the rating of external customers and Mercator Pika card holders.

Measures prepared in case of a considerable increase in risk include above all obtaining appropriate security, introduction of more strict control of customers in default, more active collecting procedures, and, if required, establishment of an expert rating department that would evaluate and monitor credit risk systematically.

Maximum exposure to credit risk for trade receivables and loans at the reporting date by geographic region was as follows:

EUR thousand	2012	2011
Slovenia	146,271	154,510
Foreign markets	146,600	156,716
Total	**292,871**	**311,226**

Maximum exposure to credit risk for trade receivables and loans at the reporting date by type of customer was as follows:

EUR thousand	2012	2011
Retail customers	84,462	92,310
Wholesale customers	104,588	106,237
Receivables from employees and the government	35,634	28,372
Deferred costs	7,434	7,572
Accrued revenues	7,880	8,911
Loans and deposits	52,873	67,824
Total	**292,871**	**311,226**

In the category of retail partners the Group included receivables from individuals related to purchases in company retail units with Mercator Pika card; the category of wholesale and other partners includes all receivables from sale of goods, material, and services, to legal/corporate entities, and receivables from employees and government bodies.

Security of receivables and loans (in gross amounts, without the impairment of receivables):

EUR thousand	2012	2011
Trade receivables	228,128	253,616
Secured receivables	144,630	165,298
Unsecured receivables	83,498	88,318
Other receivables and loans	103,821	93,880
Total	**331,949**	**347,496**

Trade receivables are secured with bank guarantees, paid collaterals, cash deposits, prime mortgages, and liabilities to these customers. Among other receivables, the Group reports receivables from banks, credit card issuers, government, employees, as well as deferred costs and accrued expenses.

Revenues from any individual customer do not reach 10% of total revenues of the Group.

Impairment of receivables

Ageing of trade receivables and loans at the reporting date:

EUR thousand	Gross value 2012	Impairment 2012	Gross value 2011	Impairment 2011
Not past due	233,442	–	265,484	–
Past due 0-60 days	43,477	774	30,833	19
Past due 61-74 days	5,845	1,145	2,818	649
Past due 75-89 days	4,193	1,462	1,884	677
More than 90 days	44,992	35,697	46,477	34,925
Total	**331,949**	**39,078**	**347,496**	**36,270**

Increase in receivables overdue by 60 days or more is a result of increased occurrence of delinquency (late payments). In 2012, activities for obtaining prime payment protection insurance were additionally intensified.

Changes in revaluation adjustment to receivables and loans:

EUR thousand	2012	2011
As at January 1	**36,270**	**34,627**
Effect of exchange rate movements	(507)	(1)
Impairment loss recognized during the year	13,749	6,320
Receivable write-off	(7,883)	(2,146)
Decrease of allowance for impairment during the year	(2,551)	(2,417)
Impairment of divested subsidiaries	–	(113)
As at December 31	**39,078**	**36,270**

The quality of receivables and loans is rated based on the policies specified by the Risk Management Council. Credit risk is monitored by classifying the trade receivables based on their characteristics.

Guarantees

Parent company is providing guarantees to its subsidiaries for borrowings from banks, in the amount of EUR 391,618 thousand.

Liquidity risk

Liquidity risk is the risk that the Group will in the course of its business activities encounter difficulties in settlement of its current liabilities which are settled in cash or with other financial assets. The Group ensures its liquidity so that it always has ample liquid assets to meet its obligations in due time, both in normal as well as challenging circumstances, without the occurrence of unacceptable losses or decline in the Group's reputation. The financial crisis that has continued and grown worse in 2012 has significantly reduced the lending activity of banks. Also, the risk that banks will not refinance existing financial liabilities incurred by non-financial firms has occurred.

The Group actively manages liquidity risk by:

- operating a centralized cash management system,
- statistically supported forecasting of cash flows,
- daily contact with its largest wholesale customers, thereby increasing the predictability of its cash flows,
- operating a centralized cash pooling system.

As at December 31, 2012 Mercator Group had access to the following liquidity lines:

EUR thousand	2012
Cash and cash equivalents	38,012
Bank deposits	2,289
Standby revolving credit lines	18,578
	58,879

In debt management, Mercator Group considered the increase in refinancing risk in financial markets and signed with the majority of banks an agreement to establish a new long-term structure of financing sources by mid 2013. One of the key elements of the final agreement which is to be based on aligning cash flows available for debt repayment with financial liabilities, will be hedging of refinancing risk, which will improve Mercator Group's financial stability.

Following is an overview of the contractual maturity of liabilities and estimated interest expenses.

2012			Up to 6 months		6 to 12 months		1-3 years		3-5 years		Over 5 years	
EUR thousand	Carrying amount	Contractual cash flow	Redemption	Interest	Redemption	Interest	Redemption	Interest	Redemption	Interest	Redemption	Interest
Non-derivative financial liabilities												
Bank borrowings	866,579	911,569	284,155	15,111	171,826	9,698	338,883	17,067	66,528	2,825	5,187	289
Borrowings from other companies	19,739	20,173	19,734	434	5	–	–	–	–	–	–	–
Finance lease liabiities	208,402	233,464	7,596	2,857	17,563	2,745	60,514	7,849	38,114	5,007	84,615	6,604
Trade and other payables and current tax liabilities	675,483	675,483	673,021	–	–	–	2,462	–	–	–	–	–
Total	**1,770,203**	**1,840,689**	**984,506**	**18,402**	**189,394**	**12,443**	**401,859**	**24,916**	**104,642**	**7,832**	**89,802**	**6,893**

2011			Up to 6 months		6 to 12 months		1-3 years		3-5 years		Over 5 years	
EUR thousand	Carrying amount	Contractual cash flow	Redemption	Interest	Redemption	Interest	Redemption	Interest	Redemption	Interest	Redemption	Interest
Non-derivative financial liabilities												
Bank borrowings	945,720	1,033,278	178,255	21,079	155,106	16,310	413,022	38,218	188,022	11,280	11,315	671
Borrowings from other companies	16,451	16,525	16,437	74	5	–	9	–				
Finance lease liabilities	222,562	267,252	7,342	4,174	6,924	4,253	68,445	14,497	37,180	8,640	102,671	13,126
Trade and other payables and current tax liabilities	586,858	586,858	584,489	–	–	–	2,369	–	–	–	–	–
Total	**1,771,591**	**1,903,913**	**786,523**	**25,327**	**162,035**	**20,563**	**483,845**	**52,715**	**225,202**	**19,920**	**113,986**	**13,797**

Market risks

Market risk is risk that is common to the entire class of assets and liabilities. Market risk is deemed to exist when there is probability that the value of investments or financial assets in a certain period of time will decrease due to changes in economic environment or other events affecting the market.

The Group uses derivative financial instruments to hedge certain market risk exposures. In these activities the Group employs hedge accounting.

Interest rate risk

Interest rate risk of the Group derives from financial liabilities. Financial liabilities expose the Group to cash flow interest rate risk.

The Group is exposed to interest rate risk as its liabilities and assets include such liabilities and assets that are sensitive to changes in interest rates, which means that some of the financial liabilities are linked to the variable interest rate EURIBOR. EURIBOR is changing on a daily basis, as it is subject to market fluctuations; this can lead to increased finance expenses for the Group. Consequently, the Group is managing and controlling the increase of finance expenses in an appropriate centralized manner. Group policy is to have at least 50% of financial liabilities that finance non-current assets hedged, and at least 25% of all financial liabilities hedged.

Exposure

The following table presents the Group's exposure to interest rate risk:

	December 31, 2012		December 31, 2011	
EUR thousand	Weighted average interest rate	Carrying amount	Weighted average interest rate	Carrying amount
Fixed rate instruments				
Financial assets	4.74	48,000	4.74	67,824
Financial liabilities	5.69	(158,845)	5.10	(106,703)
Total		**(110,845)**		**(38,879)**
Variable rate instruments				
Financial assets	–	4,874	–	–
Financial liabilities	3.33	(935,875)	4.28	(1,078,030)
Total		**(931,001)**		**(1,078,030)**

Fair value sensitivity analysis for fixed rate instruments

The Group does not hold any fixed rate financial instruments at fair value through profit or loss, nor derivative financial instruments designated as hedging instruments under a fair value hedge accounting model. Therefore, a change in interest rates at the reporting date would not affect profit or loss.

Cash flow sensitivity analysis for variable rate instruments

A change of 100 basis points in interest rates at the reporting date would have increased (decreased) profit or loss and equity by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant. The analysis is performed on the same basis for 2011.

	Profit (loss)		Equity	
EUR thousand	100 bp increase	Decrease to 0%	100 bp increase	100 bp decrease
2012				
Variable rate instruments	(9,310)	2,564	–	–
Interest rate swaps and caps	1,750	(560)	1,316	(1,467)
Cash flow sensitivity (net)	**(11,313)**	**(1,749)**	**1,316**	**(1,467)**
2011				
Variable rate instruments	(10,780)	10,780	–	–
Interest rate swaps and caps	1,750	(1,750)	4,613	(4,512)
Cash flow sensitivity (net)	**(9,030)**	**9,030**	**4,613**	**(4,512)**

Currency risk

Mercator's operations in an international environment necessarily involve exposure to currency risk. Mercator Group is facing currency risk in the markets of Serbia, Croatia and Albania; exposure to risk has increased on these two markets according to estimate.

In case of an increase in exposure to this type of risk, the Group has prepared a general policy of risk management that involves the following two steps:

- constant monitoring of macroeconomic background against which the movement of a particular exchange rate is taking place, and the related macroeconomic aspects and trends,
- adapting the operations based on the general trends and expectations, towards lesser exposure to currency risk.

In case of increased risk, the Group will decide with regard to implementation of any further measures based on the estimated level of exposure; needless to say, such measure will only be implemented following a thorough analysis and with consideration of the 'cost-benefit' principle. The type of measure will depend on its appropriateness or viability, the nature of exposure, planned Group operations, and anticipated economic effects. There are no effective instruments to hedge currency risk; therefore, the Group is currently primarily using so-called natural hedging or matching.

Exposure to currency risk

The Group's exposure to foreign currency risk was as follows:

December 31, 2012

EUR thousand	EUR*	HRK	RSD	BAM	BGN	ALL
Trade and other receivables	165,481	56,227	59,073	11,021	320	749
Available-for-sale financial assets	1,018	47	–	4	–	–
Cash and cash equivalents	13,834	2,878	18,730	1,397	402	772
Financial liabilities	(1,038,535)	(26,611)	(1,723)	(27,851)	–	–
Trade and other payables	(365,072)	(113,583)	(148,096)	(36,738)	(10,042)	(1,788)
Balance sheet exposure	**(1,223,274)**	**(81,042)**	**(72,017)**	**(52,168)**	**(9,320)**	**(268)**
Estimated sales	1,753,023	388,295	556,706	202,502	–	–
Estimated purchasing	(1,337,031)	(322,285)	(487,006)	(176,096)	–	–
Estimated transaction exposure	**415,993**	**66,010**	**69,700**	**26,406**	**–**	**–**
Forward exchange contracts	–	–	–	–	–	–
Net exposure	**(807,281)**	**(15,032)**	**(2,317)**	**(25,761)**	**(9,320)**	**(268)**

* EUR is the functional currency and it does not represent the exposure to currency risk; HRK (Croatian kuna), RSD (Serbian dinar), BAM (Bosnian convertible mark), BGN (Bulgarian lev), ALL (Albanian lek).

Mercator Group does not hold any derivative financial instruments for currency risk hedging (forward exchange contracts) as at December 31, 2011.

December 31, 2011 EUR thousand	EUR	HRK	RSD	BAM	BGN	ALL
Trade and other receivables	163,138	73,094	69,116	4,733	889	256
Available-for-sale financial assets	2,458	170	–	–	–	–
Cash and cash equivalents	11,104	2,332	12,419	1,165	272	248
Financial liabilities	(1,151,472)	(26,892)	–	(6,369)	–	–
Trade and other payables	(332,256)	(102,280)	(131,997)	(17,274)	(2,142)	(909)
Balance sheet exposure	**(1,307,028)**	**(53,576)**	**(50,462)**	**(17,745)**	**(981)**	**(405)**
Estimated sales	1,682,016	405,985	565,026	194,638	11,950	5,539
Estimated purchasing	(1,254,171)	(341,416)	(501,743)	(161,682)	(10,489)	(4,542)
Estimated transaction exposure	**427,845**	**64,569**	**63,283**	**32,956**	**1,461**	**997**
Forward exchange contracts	–	–	–	–	–	–
Net exposure	**(879,183)**	**10,993**	**12,821**	**15,211**	**480**	**592**

The following significant exchange rates applied during the year:

	Average rate		Reporting date spot rate	
Units per EUR	2012	2011	2012	2011
HRK	7.522	7.439	7.558	7.537
RSD	112.996	101.910	113.390	103.630
BAM, BGN	1.956	1.956	1.956	1.956
ALL	139.275	140.733	139.830	140.840

Sensitivity analysis

A change in the exchange rate of local currencies against the Euro at December 31 would have increased (decreased) profit or loss by the amounts shown below. A change in exchange rate would not affect the Group's equity. This analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2011.

EUR thousand	Change in exchange rate	(Estimated) transaction exposure Profit (loss)		Balance sheet exposure Profit (loss)	
2012					
HRK	**-+5%**	3,474	(3,143)	(4,265)	3,859
RSD	**-+10%**	7,744	(6,336)	(8,002)	6,547
BAM, BGN	**-+5%**	1,390	(1,257)	(2,746)	2,484
ALL	**-+5%**	–	–	(14)	13
2011					
HRK	**-+5%**	3,398	(3,075)	(2,820)	2,551
RSD	**-+10%**	6,662	(6,026)	(5,312)	4,806
BAM, BGN	**-+5%**	1,811	(1,639)	(986)	892
ALL	**-+5%**	52	(47)	(21)	19

Capital management

Policy of the Group is oriented to achieving adequate amount of capital so as to maintain investor, creditor and market confidence and to sustain future development of the business. Management Board therefore monitors on an ongoing basis the return on capital and capital structure.

The target capital structure ratio between equity and net financial debt of the Group is 1:1.5. As at reporting date, the said ratio was as follows:

EUR thousand	2012	2011 restated
Financial liabilities and liabilities for derivative financial instruments	1,099,989	1,189,295
Less:		
Loans and deposits	52,873	67,824
Available-for-sale financial assets	1,069	2,628
Derivative financial instruments	1	158
Cash and cash equivalents	38,012	27,540
Net financial debt	**1,008,034**	**1,091,145**
Equity (ordinary shares)	**663,249**	**756,457**
Ratio between equity and net financial debt	1:1.5	1:1.4

As at December 31, 2012 the company Poslovni sistem Mercator, d.d., held 42,192 treasury shares (2011: 42,192 treasury shares).

Accounting for derivative financial instruments

The Group has signed several agreements on interest rate swaps and interest rate caps, exclusively for the purposes of hedging; all criteria relevant to such purposes are met. The instruments employed are intended for cash flow hedging and are highly effective in managing the cash flows related to Group's borrowings.

Upon completion of a transaction, Mercator Group documents the relation between derivative financial instruments and hedged items, as well as the risk management goal and strategy for effecting various hedging transactions. This process also includes relating all derivative financial instruments to the portfolio of borrowings, or to particular borrowings.

The Group also documents every estimate it makes, both upon the completion of a transaction, as well as later, with regard to the effectiveness of derivative financial instruments employed for hedging, in managing the cash flow from borrowings.

The Group employs derivative financial instruments for hedging purposes and recognizes them initially at fair value. If the cash flow hedge is effective, the changes in fair value are recognized directly in equity; otherwise, they are recognized in the profit or loss for the current period. The method for recognizing the profit or loss related to these instruments does not depend on the form of the hedged item.

Mercator Group manages financial risks in the framework of adopted policy centrally at the parent company level which enters into interest rate swap contracts at market terms (arm's length principle) based on specific policies for managing specific risks.

The following table indicates the periods in which the cash flows associated with derivatives that are cash flow hedges are expected to occur and their impact on profit or loss.

2012

EUR thousand	Carrying amount	Contractual cash flow	1 year or less	1-2 years	2-5 years	Over 5 years
Interest rate swaps and caps						
Assets	1	1	–	–	1	–
Liabilities	(5,269)	(5,792)	(3,679)	(2,113)	–	–

2011

EUR thousand	Carrying amount	Contractual cash flow	1 year or less	1-2 years	2-5 years	Over 5 years
Interest rate swaps and caps						
Assets	158	–	–	–	–	–
Liabilities	(4,562)	(4,574)	(1,351)	(2,159)	(1,064)	–

Fair values

Fair values of assets and liabilities and carrying amounts as shown in the balance sheet:

	December 31, 2012		December 31, 2011 restated	
EUR thousand	Carrying amount	Fair value	Carrying amount	Fair value
Derivative financial instruments	(5,268)	(5,268)	(4,404)	(4,404)
Trade and other receivables	239,998	239,998	243,402	243,402
Current tax assets	6,462	6,462	4,062	4,062
Loans and deposits	52,873	52,170	67,824	66,922
Available-for-sale financial assets	1,069	1,069	2,628	2,628
Cash and cash equivalents	38,012	38,012	27,540	27,540
Fixed rate bank borrowings	(158,845)	(156,732)	(106,703)	(105,284)
Floating rate bank borrowings	(707,734)	(707,734)	(839,017)	(839,017)
Borrowings from other companies	(19,739)	(19,739)	(16,451)	(16,451)
Finance lease	(208,402)	(208,402)	(222,562)	(222,562)
Trade and other payables	(675,320)	(675,320)	(586,351)	(586,351)
Current tax liabilities	(163)	(163)	–	–

Fair values of non-derivative financial liabilities are not determined, as the carrying amount represents a reasonable approximation of fair value.

Fair value of loans (granted) and borrowings is calculated based on discounted cash flow of the principal and interest. A 5% p.a. rate is considered as the discount rate for both years. According to the Group's estimate, a 5-year loan could be taken out at this rate at the end of the period.

Fair value of derivative financial instruments was calculated as the present value of estimated future cash flows. Calculation of the fair value changes of each instrument is assessed on a semi-annual basis and recognized in the income statement when the hedged transaction affects the income statement.

Fair value hierarchy

Based on the calculation of their fair value, financial instruments are divided into two levels:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

2012

EUR thousand	**Level 1**	**Level 2**	**Total**
Available-for-sale financial assets	338	–	338
Derivative financial instruments - assets	–	1	1
Derivative financial instruments - liabilities	–	(5,269)	(5,269)

2011

EUR thousand	**Level 1**	**Level 2**	**Total**
Available-for-sale financial assets	1,885	–	1,885
Derivative financial instruments - assets	–	158	158
Derivative financial instruments - liabilities	–	(4,562)	(4,562)

Available-for-sale financial assets also include investments valued at historical cost in the amount of EUR 731 thousand.

30. Operating leases

Minimum lease payments pertaining to operating lease (Group as the lessee) are as follows:

EUR thousand	**2012**	**2011**
Less than one year	33,840	31,295
Between one and five years	133,451	118,933
More than five years	221,240	225,097
Total	**388,531**	**375,325**

Rents are mostly agreed upon in fixed terms, i.e. their amount does not depend on the revenue generated in leased stores.

31. Capital commitments

Capital expenditures (investment into property, plant and equipment) agreed upon and specified in contracts and agreements, which were not yet recognized in the balance sheet as at the balance sheet cut-off date:

EUR thousand	2012	2011
Property, plant, and equipment	2,732	27,280

32. Contingencies

Group contingencies also include guarantees provided in the amount of EUR 6,270 thousand (2011: EUR 13,120 thousand).

Tax authorities may, in the period of five or ten years after the tax return date, review the operations of the companies in the Group, which may result in additional taxation, including the liability of default interest payment and penalty related to corporate income tax or other taxes and duties. Group companies are not aware of any circumstances that could result in any such liability.

33. Related party transactions

The company Mercator, d.d., does not have a controlling owner or shareholder. Companies of the Pivovarna Laško Group are the largest shareholder, holding 23.34% of the total equity.

Related parties of the Group are its management personnel. Included in the management personnel are members of Management Boards and Supervisory Boards in the companies of Mercator Group.

New Supervisory Board members were appointed in March 2012; they, in turn, appointed the new Management Board.

As at the end of the year, managerial staff held 36 shares of the company Mercator, d.d., which represents 0.001 % of total equity.

In 2012, the Group paid out the following compensation in gross amounts to Management Board members and Supervisory Board members of group companies:

EUR thousand		2012		2011
	Amount	Number of recipients	Amount	Number of recipients
Members of Management Boards of companies in Mercator Group	2,092	32	2,954	32
- basic salaries	1,941	32	2,404	32
- performance bonuses	–	–	403	30
- other employment benefits	151	32	147	32
Members of the Supervisory Board of the Mercator Group companies	207	16	282	12
Total	**2,299**	**48**	**3,236**	**44**

Members of Supervisory Boards at Mercator Group subsidiaries do not receive any compensation for their work; therefore the disclosed amounts refer solely to the parent company.

The number of Supervisory Board members at Mercator Group companies increased among the recipients in 2012 due to appointment of new Supervisory Board members at the parent company; therefore, list of recipients includes both previous and new Supervisory Board members.

Gross payments to Management Board and Supervisory Board members of companies in Mercator Group represent 0.8% of total employee benefit expenses (2011: 1.1%).

Gross payments to Mercator, d.d., Management Board in 2012:

2012						
EUR thousand	**First and last name**	**Total payments**	**Gross payment**	**Base salary**	**Performance bonuses**	**Other payments**
President of the Management Board	Anton Balažič	107	96	96	–	11
President of the Management Board	Žiga Debeljak	119	106	106	–	13
Senior Vice President	Drago Kavšek	95	85	85	–	10
Senior Vice President	Igor Maroša	84	75	75	–	9
Senior Vice President	Stanka Pejanović	156	138	138	–	18
Senior Vice President	Vera Aljančič Falež	68	60	60	–	8
Senior Vice President	Peter Zavrl	70	60	60	–	10
Senior Vice President	Mateja Jesenek	27	24	24	–	3
Senior Vice President	Melita Kolbezen	121	106	106	–	15
		847	**750**	**750**	**–**	**97**

Reported payments to Management Board members include payments for performance of duties of the Management Board member; they do not include payments received after the termination of such position.

Gross payments to Management Board and Supervisory Board members in 2012 represent 0.65% of total labour costs at the company Mercator, d.d. (2011: 0.87%).

Gross compensation paid to members of managerial and supervisory bodies at the parent company in 2012 are reported in the following two tables (disclosure pursuant to Article 294 of the Companies Act):

(in EUR)	Participation in profit	Options	Performance bonuses	Cost/expenses reimbursement	Insurance premiums	Commissions	Other additional income	TOTAL
MANAGEMENT BOARD	**–**	**–**	**–**	**4,536**	**35,539**	**–**	**56,740**	**96,816**
Anton Balažič	–	–	–	470	–	–	10,257	10,727
Žiga Debeljak	–	–	–	526	8,000	–	4,494	13,020
Drago Kavšek	–	–	–	478	–	–	9,548	10,026
Igor Maroša	–	–	–	470	–	–	8,383	8,853
Stanka Pejanović	–	–	–	–	10,739	–	7,079	17,818
Mateja Jesenek	–	–	–	206	1,600	–	945	2,752
Vera Aljančič Falež	–	–	–	886	4,000	–	3,774	8,660
Peter Zavrl	–	–	–	819	4,000	–	5,019	9,838
Melita Kolbezen	–	–	–	681	7,200	–	7,241	15,122

(in EUR)	GROSS PAYMENT	Payment for performance of duties	Session attendance fees	OTHER PAYMENTS	Participation in profit	Options	Other rewards	Cost/expense reimbursement	Insurance premiums	Commissions	Other additional income
SUPERVISORY BOARD	**206,503**	**169,500**	**37,003**	–	–	–	–	–	–	–	–
Lahovnik Matej	27,468	22,500	4,968	–	–	–	–	–	–	–	–
Rozman Rok	16,605	13,500	3,105	–	–	–	–	–	–	–	–
Galić Boris	17,914	13,500	4,414	–	–	–	–	–	–	–	–
Podlesnik Zdenko	16,176	13,500	2,676	–	–	–	–	–	–	–	–
Zevnik Marjeta	16,339	13,500	2,839	–	–	–	–	–	–	–	–
Sandi Leban	22,720	18,000	4,720	–	–	–	–	–	–	–	–
Mateja Širec	21,910	18,000	3,910	–	–	–	–	–	–	–	–
Ivan Valand	22,844	18,000	4,844	–	–	–	–	–	–	–	–
Robert Šega	8,403	7,500	903	–	–	–	–	–	–	–	–
Jadranka Dakič	5,016	4,500	516	–	–	–	–	–	–	–	–
Jože Cvetek	5,016	4,500	516	–	–	–	–	–	–	–	–
Janez Strniša	5,016	4,500	516	–	–	–	–	–	–	–	–
Kristjan Verbič	5,016	4,500	516	–	–	–	–	–	–	–	–
Štefan Vavti	5,741	4,500	1,241	–	–	–	–	–	–	–	–
Ivica Župetič	5,303	4,500	803	–	–	–	–	–	–	–	–
Miro Medvešek	5,016	4,500	516	–	–	–	–	–	–	–	–

in EUR

AUDIT COMMITTEE	**48,295**	**39,750**	**8,545**	–	–	–	–	–	–	–	–
Zevnik Marjeta	13,508	11,250	2,258	–	–	–	–	–	–	–	–
Rozman Rok	8,522	6,750	1,772	–	–	–	–	–	–	–	–
Igličar Aleksander	8,040	6,750	1,290	–	–	–	–	–	–	–	–
Slapničar Sergeja	8,040	6,750	1,290	–	–	–	–	–	–	–	–
Jadranka Dakič	4,653	3,750	903	–	–	–	–	–	–	–	–
Jože Cvetek	2,766	2,250	516	–	–	–	–	–	–	–	–
Peter Ribarič	2,766	2,250	516	–	–	–	–	–	–	–	–

in EUR

HUMAN RESOURCE COMMITTEE	**53,621**	**45,000**	**8,621**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Širec Mateja	8,048	6,750	1,298	–	–	–	–	–	–	–	–
Galić Boris	8,069	6,750	1,319	–	–	–	–	–	–	–	–
Lahovnik Matej	8,040	6,750	1,290	–	–	–	–	–	–	–	–
Podlesnik Zdenko	8,011	6,750	1,261	–	–	–	–	–	–	–	–
Rozman Rok	13,413	11,250	2,163	–	–	–	–	–	–	–	–
Zevnik Marjeta	8,040	6,750	1,290	–	–	–	–	–	–	–	–

Gross compensation paid to members of managerial and supervisory bodies at subsidiaries in 2012 are reported in the following table (disclosure pursuant to Article 294 of the Companies Act):

(in EUR)	Companies at which the duties are performed	GROSS PAYMENT	Fixed part	Variable part	OTHER PAYMENTS	Participation in profit	Options	Other rewards	Cost/expense reimbursement	Insurance premiums	Commissions	Other additional income	TOTAL
Ivica Župetić	Mercator - H, d.o.o.	15,213	15,213	–	109			109	–	–	–	15,322	15,213
TOTAL		**15,213**	**15,213**	**–**	**109**	**–**	**–**	**109**	**–**	**–**	**–**	**15,322**	**15,213**

The compensation pertains to the period when Mr Ivica Župetić was a Supervisory Board member at the company. Other members of managerial and supervisory bodies at Mercator, d.d., did not receive any payment for performance of duties at the company's subsidiaries.

34. Major events following the end of the year at hand

As a part of the project of monetizing a part of our real property, we obtained in 2012 binding offers of short-listed investors, and completed the research stage in which we examined the possibilities of carrying out the monetization project. The answers we got were inconclusive and we decided early in 2013 to postpone the monetization project for the time being. Mercator has prepared the basis for instant resumption of the project in case the macroeconomic situation improves and ownership composition at Mercator is stabilized.

Independent Auditor's Report

KPMG

Independent Auditor's Report

To the Shareholders of Poslovni sistem Mercator, d.d., Ljubljana

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of the company Poslovni sistem Mercator, d.d., Ljubljana and its subsidiaries (the Mercator Group), which comprise the consolidated balance sheet as at 31 December 2012, the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards as adopted by EU, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Mercator Group as at 31 December 2012, its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by EU.

Report on Other Legal and Regulatory Requirements

As required by the Slovenian Companies Act we herewith confirm that the information in the management report is in conformity with the accompanying financial statements.

KPMG SLOVENIJA,
podjetje za revidiranje, d.o.o.

Jason Stachurski, B.Sc.Ec.
Certified Auditor

Ljubljana, 1 March 2013

Partner

KPMG Slovenija, d.o.o.
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FINANCIAL REPORT OF THE COMPANY POSLOVNI SISTEM MERCATOR, D.D.

Balance sheet

EUR thousand	Dec 31, 2012	Dec 31, 2011 restated	Jan 1, 2011 restated
ASSETS			
Non-current assets			
Property, plant, and equipment	1,035,658	1,003,846	1,014,704
Investment property	3,194	3,450	3,894
Intangible assets	9,570	10,513	9,652
Deferred tax assets	19,200	11,594	11,190
Trade and other receivables	-	-	-
Loans and deposits	268	870	286
Investment into equity of subsidiaries	557,881	636,319	618,813
Available-for-sale financial assets	928	2,399	3,547
	1,626,699	**1,668,991**	**1,662,086**
Current assets			
Inventories	84,225	136,003	136,429
Trade and other receivables	138,532	163,118	158,907
Current tax assets	4,962	2,167	5
Loans and deposits	54,206	34,575	48,848
Derivative financial instruments	1	158	70
Cash and cash equivalents	11,611	10,068	3,829
	293,537	**346,089**	**348,088**
Total assets	**1,920,236**	**2,015,080**	**2,010,174**
EQUITY			
Share capital	157,129	157,129	157,129
Share premium	198,872	198,872	198,872
Treasury shares	(3,235)	(3,235)	(3,235)
Revenue reserves	171,984	239,249	223,492
Fair value reserve	215,494	190,650	194,435
Retained earnings	-	13,246	3,612
Profit (loss) for the year	-	15,574	36,806
	740,244	**811,485**	**811,111**
LIABILITIES			
Non-current liabilities			
Trade and other payables	1,599	2,022	2,447
Borrowings and other financial liabilities	436,941	628,686	456,547
Deferred tax liabilities	40,870	39,805	40,814
Provisions	44,101	26,926	29,459
	523,511	**697,439**	**529,267**
Current liabilities			
Trade and other payables	324,733	306,686	341,239
Current tax liabilities	-	-	5,759
Borrowings and other financial liabilities	326,479	194,908	320,320
Derivative financial instruments	5,269	4,562	2,478
	656,481	**506,156**	**669,796**
Total liabilities	**1,179,992**	**1,203,595**	**1,199,063**
Total equity and liabilities	**1,920,236**	**2,015,080**	**2,010,174**

Income statement

EUR thousand	2012	2011 restated
Revenue	1,425,391	1,579,669
Cost of goods sold and selling costs	(1,329,650)	(1,453,521)
Administrative expenses	(80,495)	(57,276)
Impairment of property, equipment, and intangible assets	(9,780)	-
Other income	13,560	10,922
Results from operating activities	**19,026**	**79,794**
Finance income	8,318	9,411
Finance expenses	(111,218)	(50,378)
Net finance expenses	**(102,900)**	**(40,967)**
Profit before income tax	**(83,874)**	**38,827**
Corporate income tax	6,272	(7,496)
Profit (loss) for the year	**(77,602)**	**31,331**
Basic and diluted (loss) earnings per share in EUR	(20.8)	8.4

* Due to the transfer of a part of operating activities to the company M – Tehnika, d.d., in 2012, the income statements are not fully comparable between the periods. Performance analysis should only be based on consolidated income statement which represents the performance of the Mercator Group as a uniform business entity.

Statement of comprehensive income

EUR thousand	2012	2011 restated
Profit (loss) for the year	(77,602)	31,331
Other comprehensive income		
Change in fair value of available-for-sale financial assets	(120)	(1,159)
Disposal of available-for-sale financial assets transferred to profit or loss	699	-
Change in fair value of cash flow hedges	(864)	(2,780)
Change in fair value of investment into equity of subsidiaries	(21,691)	4,585
Change in fair value of real estate	46,984	-
Decrease (increase) on disposal of subsidiaries	3,115	(2,981)
Deferred taxes	577	1,163
Other comprehensive income for the year	**28,700**	**(1,172)**
Total comprehensive income for the year	**(48,902)**	**30,159**

Statement of changes in equity

EUR thousand	Share capital	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Profit (loss) for the year	Total equity
As at January 1, 2011	**157,129**	**198,872**	**(3,235)**	**238,015**	**194,435**	**3,612**	**36,806**	**825,634**
Effect of changes in accounting policies				(14,523)				(14,523)
As at January 1, 2011, restated	**157,129**	**198,872**	**(3,235)**	**223,492**	**194,435**	**3,612**	**36,806**	**811,111**
Total comprehensive income for the year								
Profit (loss) for the year	-	-	-	-	-	-	31,331	31,331
Other comprehensive income	-	-	-	-	(3,785)	2,613	-	(1,172)
Total comprehensive income for the year	**-**	**-**	**-**	**-**	**(3,785)**	**2,613**	**31,331**	**30,159**
Transactions with owners directly recognized in equity								
Contributions by and distributions to owners								
Dividends to equity holders*	-	-	-	-	-	(29,785)	-	(29,785)
Total transactions with owners	**-**	**-**	**-**	**-**	**-**	**(29,785)**	**-**	**(29,785)**
Transfer of profit (loss) for the year to retained earnings	-	-	-	-	-	36,806	(36,806)	-
Distribution of profit (loss) for the year pursuant to Management Board	-	-	-	15,757	-	-	(15,757)	-
As at December 31, 2011	**157,129**	**198,872**	**(3,235)**	**239,249**	**190,650**	**13,246**	**15,574**	**811,485**

* The amount of dividend payment differs from the amount specified in the Shareholders Assembly resolution because treasury shares were included in the calculation of the required amount for dividend payment.

Statement of changes in equity (continued)

EUR thousand	Share capital	Share premium	Treasury shares	Revenue reserves	Fair value reserve	Retained earnings	Profit (loss) for the year	Total equity
As at January 1, 2012	**157,129**	**198,872**	**(3,235)**	**239,249**	**190,650**	**13,246**	**15,574**	**811,485**
Total comprehensive income for the year								
Profit (loss) for the year	-	-	-	-	-	-	(77,602)	(77,602)
Other comprehensive income	-	-	-	-	24,844	3,856	-	28,700
Total comprehensive income for the year	**-**	**-**	**-**	**-**	**24,844**	**3,856**	**(77,602)**	**(48,902)**
Transactions with owners directly recognized in equity								
Contributions by and distributions to owners								
Dividends to equity holders*	-	-	-	-	-	(22,339)	-	(22,339)
Total transactions with owners	**-**	**-**	**-**	**-**	**-**	**(22,339)**	**-**	**(22,339)**
Transfer of profit (loss) for the year to retained earnings	-	-	-	-	-	15,574	(15,574)	-
Distribution of revenue reserves pursuant to Management Board	-	-	-	(67,265)		(10,337)	77,602	-
As at December 31, 2012	**157,129**	**198,872**	**(3,235)**	**171,984**	**215,494**	**-**	**-**	**740,244**

* The amount of dividend payment differs from the amount specified in the Shareholders Assembly resolution because treasury shares were included in the calculation of the required amount for dividend payment.

Proposal on the allocation of distributable profit

Distributable profit for 2012 consists of the following:

(in EUR)	
Profit (loss) for the year 2012	(77,602,465.26)
Loss for the year covered from retained earnings	10,337,126.70
Loss for the year covered from other revenue reserves	67,265,338.56
Distributable profit for the year	-

The company covered loss for the year from retained earnings and other revenue reserves.

Statement of cash flows

EUR thousand	2012	2011 restated
Cash flows from operating activities		
Profit (loss) for the year	**(77,602)**	**31,331**
Adjustments:		
Income tax expenses	(6,272)	7,496
Depreciation of property, plant and equipment	35,953	35,531
Depreciation of investment property	140	160
Amortization of intangible assets	3,733	3,743
Impairment losses of goodwill	691	-
Impairment losses on property, plant, and equipment, intangible assets, and (gains) losses on disposal	8,584	(189)
Change in provisions	19,666	(1,085)
Looses on investments in subsidiaries	66,058	-
Profit (loss) on disposal of available-for-sale financial assets	480	(3,992)
Dividend received and impairment of available-for-sale financial assets	(1,401)	-
Interest received	(5,155)	(5,001)
Interest paid	36,041	48,013
	80,916	**116,007**
Change in inventories	52,074	426
Change in trade and other receivables	22,049	(5,175)
Change in trade and other payables	13,206	(43,309)
Interest paid	(36,041)	(48,013)
Income tax paid	-	(6,978)
Net cash from operating activities	**132,204**	**12,958**
Cash flows from investing activities		
Acquisition of subsidiaries and business operations	(27,075)	(21,974)
Acquisition of property, plant and equipment and investment property	(34,728)	(31,432)
Acquisition of intangible assets	(3,485)	(4,604)
Acquisition of available-for-sale financial assets	(5)	-
Loans and deposits made	(77,135)	(103,411)
Disposal of subsidiaries	19,117	10,000
Proceeds from sale of property, plant, and equipment and investment property	9,570	5,856
Proceeds from sale of intangible assets	16	1
Proceeds from sale of available-for-sale financial assets	1,608	-
Interest received	5,155	5,001
Dividends income	1,371	54
Loans and deposits repayments received	58,113	117,101
Net cash used in investing activities	**(47,478)**	**(23,408)**
Cash flows from financing activities		
Repayment of non-current borrowings	(107,825)	(127,214)
Increase in non-current borrowings	27,459	299,353
(Repayment) increase in current borrowings	19,346	(125,412)
Dividend paid	(22,163)	(30,038)
Net cash from financing activities	**(83,183)**	**16,689**

Net increase (decrease) in cash and cash equivalents	**1,543**	**6,239**
Cash and cash equivalents as at beginning of the year	10,068	3,829
Cash and cash equivalents as at end of the year	**11,611**	**10,068**

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